

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D. C. 20549

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the Quarter Ended March 31, 2002  
Commission File No. 1-8968**

**ANADARKO PETROLEUM CORPORATION**

1201 Lake Robbins Drive, The Woodlands, Texas 77380-1046  
(832) 636-1000

Incorporated in the  
State of Delaware

Employer Identification  
No. 76-0146568

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes X No \_\_\_\_\_

The number of shares outstanding of the Company's common stock as of April 30, 2002 is shown below:

<b>Title of Class</b>	<b>Number of Shares Outstanding</b>
Common Stock, par value \$0.10 per share	248,319,002

## TABLE OF CONTENTS

	<u>Page</u>
<b>PART I</b>	
Item 1. Financial Statements	
<a href="#"><u>Consolidated Statement of Income for the Three Months Ended March 31, 2002 and March 31, 2001</u></a>	3
<a href="#"><u>Consolidated Balance Sheet as of March 31, 2002 and December 31, 2001</u></a>	4
<a href="#"><u>Consolidated Statement of Comprehensive Income for the Three Months Ended March 31, 2002 and March 31, 2001</u></a>	6
<a href="#"><u>Consolidated Statement of Cash Flows for the Three Months Ended March 31, 2002 and March 31, 2001</u></a>	7
<a href="#"><u>Notes to Consolidated Financial Statements</u></a>	8
Item 2. <a href="#"><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></a>	25
Item 3. <a href="#"><u>Quantitative and Qualitative Disclosures About Market Risk</u></a>	35
<b>PART II</b>	
Item 1. <a href="#"><u>Legal Proceedings</u></a>	43
Item 6. <a href="#"><u>Exhibits and Reports on Form 8-K</u></a>	43

## PART I. FINANCIAL INFORMATION

### Item 1. Financial Statements

#### ANADARKO PETROLEUM CORPORATION CONSOLIDATED STATEMENT OF INCOME (Unaudited)

	Three Months Ended March 31	
	<u>2002</u>	<u>2001</u>
<i>millions except per share amounts</i>		
<b>Revenues</b>		
Gas sales	\$ 353	\$ 1,114
Oil and condensate sales	350	361
Natural gas liquids sales	42	73
Marketing sales	607	1,458
Minerals and other	21	3
Total	<u>1,373</u>	<u>3,009</u>
<b>Costs and Expenses</b>		
Marketing purchases	596	1,433
Operating expenses	170	157
Administrative and general	72	49
Depreciation, depletion and amortization	267	274
Other taxes	56	83
Impairments related to oil and gas properties	8	7
Amortization of goodwill	--	17
Total	<u>1,169</u>	<u>2,020</u>
Operating Income	204	989
<b>Other (Income) Expense</b>		
Merger expenses	--	10
Interest expense	49	22
Other (income) expense	23	(96)
Total	<u>72</u>	<u>(64)</u>
Income Before Income Taxes	132	1,053
<b>Income Taxes</b>	<u>43</u>	<u>389</u>
<b>Net Income Before Cumulative Effect of Change in Accounting Principle</b>	<u>\$ 89</u>	<u>\$ 664</u>
Preferred Stock Dividends	<u>1</u>	<u>3</u>
<b>Net Income Available to Common Stockholders Before Cumulative Effect of Change in Accounting Principle</b>	<u>\$ 88</u>	<u>\$ 661</u>
Cumulative Effect of Change in Accounting Principle	<u>--</u>	<u>5</u>
<b>Net Income Available to Common Stockholders</b>	<u>\$ 88</u>	<u>\$ 656</u>
<b>Per Common Share</b>		
Net income - before change in accounting principle - basic	\$ 0.35	\$ 2.64
Net income - before change in accounting principle - diluted	\$ 0.34	\$ 2.52
Change in accounting principle - basic	\$ --	\$ (0.02)
Change in accounting principle - diluted	\$ --	\$ (0.02)
Net income - basic	\$ 0.35	\$ 2.62
Net income - diluted	\$ 0.34	\$ 2.50
Dividends	\$0.075	\$ 0.05
<b>Average Number of Common Shares Outstanding - Basic</b>	<u>248</u>	<u>250</u>
<b>Average Number of Common Shares Outstanding - Diluted</b>	<u>263</u>	<u>263</u>

See accompanying notes to consolidated financial statements.

**Item 1. Financial Statements (continued)**

**ANADARKO PETROLEUM CORPORATION**  
**CONSOLIDATED BALANCE SHEET**  
(Unaudited)

<i>millions</i>	March 31, <u>2002</u>	December 31, <u>2001</u>
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 26	\$ 37
Accounts receivable, net of allowance:		
Customers	560	532
Others	319	486
Other current assets	<u>125</u>	<u>146</u>
Total	<u>1,030</u>	<u>1,201</u>
<b>Properties and Equipment</b>		
Original cost (includes unproved properties of \$3,565 and \$3,573 as of March 31, 2002 and December 31, 2001, respectively)	20,862	20,088
Less accumulated depreciation, depletion and amortization	<u>6,697</u>	<u>6,451</u>
Net properties and equipment - based on the full cost method of accounting for oil and gas properties	<u>14,165</u>	<u>13,637</u>
<b>Other Assets</b>	<u>479</u>	<u>503</u>
<b>Goodwill</b>	<u>1,432</u>	<u>1,430</u>
	<u>\$ 17,106</u>	<u>\$ 16,771</u>

See accompanying notes to consolidated financial statements.

**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**CONSOLIDATED BALANCE SHEET** (continued)  
(Unaudited)

<i>millions except share amounts</i>	March 31, 2002	December 31, 2001
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 932	\$ 1,132
Accrued expenses	307	257
Current portion, notes and debentures	278	412
Total	<u>1,517</u>	<u>1,801</u>
<b>Long-term Debt</b>	<u>5,240</u>	<u>4,638</u>
<b>Other Long-term Liabilities</b>		
Deferred income taxes	3,444	3,451
Other	531	516
Total	<u>3,975</u>	<u>3,967</u>
<b>Stockholders' Equity</b>		
Preferred stock, par value \$1.00 per share (2.0 million shares authorized, 0.1 million shares issued as of March 31, 2002 and December 31, 2001)	<u>103</u>	<u>103</u>
Common stock, par value \$0.10 per share (450.0 million shares authorized, 254.3 million and 254.1 million shares issued as of March 31, 2002 and December 31, 2001, respectively)	<u>25</u>	<u>25</u>
Paid-in capital	5,349	5,336
Retained earnings	1,346	1,276
Treasury stock (3.2 million and 2.2 million shares as of March 31, 2002 and December 31, 2001, respectively)	<u>(166)</u>	<u>(116)</u>
Deferred compensation and ESOP (0.9 million shares as of March 31, 2002 and December 31, 2001)	<u>(86)</u>	<u>(96)</u>
Executives and Directors Benefits Trust, at market value (2.0 million shares as of March 31, 2002 and December 31, 2001)	<u>(114)</u>	<u>(114)</u>
Accumulated other comprehensive income (loss):		
Unrealized loss on derivatives	(20)	--
Foreign currency translation adjustments	(48)	(46)
Minimum pension liability	(15)	(3)
Total	<u>(83)</u>	<u>(49)</u>
Total	<u>6,374</u>	<u>6,365</u>
<b>Commitments and Contingencies</b>	<u>--</u>	<u>--</u>
	<u>\$ 17,106</u>	<u>\$ 16,771</u>

See accompanying notes to consolidated financial statements.

**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**  
(Unaudited)

	Three Months Ended March 31	
<i>millions</i>	<u>2002</u>	<u>2001</u>
<b>Net Income Available to Common Stockholders</b>	\$ 88	\$ 656
<b>Other Comprehensive Income (Loss), net of taxes</b>		
Unrealized gain (loss) on derivatives:		
Cumulative effect of accounting change (net of taxes of \$3 for the three months ended March 31, 2001)	--	(5)
Reclassification of cumulative effect of accounting change included in net income (net of taxes of \$(2) for the three months ended March 31, 2001)	--	3
Unrealized loss during the period (net of taxes of \$11 and \$3 for the three months ended March 31, 2002 and 2001, respectively)	(19)	(3)
Reclassification for gains included in net income (net of taxes of \$1 for the three months ended March 31, 2002)	<u>(1)</u>	<u>--</u>
Total unrealized loss on derivatives	(20)	(5)
Foreign currency translation adjustments	(2)	--
Minimum pension liability (net of taxes of \$7 and \$1 for the three months ended March 31, 2002 and 2001, respectively)	<u>(12)</u>	<u>(3)</u>
Total	<u>(34)</u>	<u>(8)</u>
<b>Comprehensive Income</b>	<u>\$ 54</u>	<u>\$ 648</u>

See accompanying notes to consolidated financial statements.

**Item 1. Financial Statements (continued)**

**ANADARKO PETROLEUM CORPORATION**  
**CONSOLIDATED STATEMENT OF CASH FLOWS**  
(Unaudited)

	Three Months Ended March 31	
<i>millions</i>	<u>2002</u>	<u>2001</u>
<b>Cash Flow from Operating Activities</b>		
Net income before cumulative effect of change in accounting principle	\$ 89	\$ 664
Adjustments to reconcile net income before cumulative effect of change in accounting principle to net cash provided by operating activities:		
Depreciation, depletion and amortization	272	274
Amortization of goodwill	--	17
Non-cash merger expenses	--	3
Interest expense – zero coupon debentures	3	3
Deferred income taxes	9	209
Impairments related to oil and gas properties	8	7
Other non-cash items	18	(60)
	<u>399</u>	<u>1,117</u>
Decrease in accounts receivable	114	239
Decrease in accounts payable and accrued expenses	(104)	(137)
Other items – net	9	(108)
Net cash provided by operating activities	<u>418</u>	<u>1,111</u>
<b>Cash Flow from Investing Activities</b>		
Additions to properties and equipment	(813)	(658)
Acquisition costs, net of cash acquired	--	(790)
Sales and retirements of properties and equipment	13	71
Net cash used in investing activities	<u>(800)</u>	<u>(1,377)</u>
<b>Cash Flow from Financing Activities</b>		
Additions to debt	1,086	682
Retirements of debt	(615)	--
Decrease in accounts payable, banks	(45)	(24)
Dividends paid	(19)	(15)
Purchase of treasury stock	(50)	--
Issuance of common stock	16	17
Net cash provided by financing activities	<u>373</u>	<u>660</u>
<b>Effect of Exchange Rate Changes on Cash</b>	<u>(2)</u>	<u>--</u>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	(11)	394
<b>Cash and Cash Equivalents at Beginning of Period</b>	<u>37</u>	<u>199</u>
<b>Cash and Cash Equivalents at End of Period</b>	<u>\$ 26</u>	<u>\$ 593</u>

See accompanying notes to consolidated financial statements.

## Item 1. Financial Statements (continued)

### ANADARKO PETROLEUM CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### 1. Summary of Accounting Policies

**General** Anadarko Petroleum Corporation is engaged in the exploration, development, production and marketing of natural gas, crude oil, condensate and natural gas liquids (NGLs). The Company also engages in the hard minerals business through non-operated joint ventures and royalty arrangements in several coal, trona (natural soda ash) and industrial mineral mines. The terms "Anadarko" and "Company" refer to Anadarko Petroleum Corporation and its subsidiaries. The principal subsidiaries of Anadarko are: RME Petroleum Company; RME Holding Company (RME); Anadarko Canada Energy Ltd.; Anadarko Canada Corporation (Anadarko Canada); RME Land Corp.; and, Anadarko Algeria Company, LLC (Anadarko Algeria). Certain amounts for the prior year have been reclassified to conform to the current presentation.

The information, as furnished herein, reflects all normal recurring adjustments that are, in the opinion of management, necessary for a fair statement of financial position as of March 31, 2002 and December 31, 2001, and for the results of operations and cash flows for the three months ended March 31, 2002 and 2001.

**Derivative Financial Instruments** In 2001, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended, which provides guidance for accounting for derivative instruments and hedging activities. The change was effective January 2001 and the related cumulative adjustment to net income was a decrease of \$8 million (\$5 million after taxes or \$0.02 per share) and the cumulative adjustment to accumulated other comprehensive income was a decrease of \$8 million (\$5 million after taxes).

Derivative financial instruments utilized to manage or reduce commodity price risk related to the Company's equity production are accounted for under the provisions of SFAS No. 133. Under this statement, all derivatives are carried on the balance sheet at fair value. Realized gains/losses and option premiums are recognized in the statement of income when the underlying physical gas and oil production is sold. Accordingly, realized derivative gains/losses are generally offset by similar changes in the realized prices of the underlying physical gas and oil production. Realized derivative gains/losses are reflected in the average sales price of the physical gas and oil production.

Accounting for unrealized gains/losses is dependent on whether the derivative financial instruments have been designated and qualify as part of a hedging relationship. Derivative financial instruments may be designated as a hedge of exposure to changes in fair values, cash flows or foreign currencies, if certain conditions are met. Unrealized gains/losses on derivative financial instruments that do not meet the conditions to qualify for hedge accounting are recognized currently in earnings.

If the hedged exposure is to changes in fair value, the gains/losses on the derivative financial instrument, as well as the offsetting losses/gains on the hedged item, are recognized currently in earnings. Consequently, if gains/losses on the derivative financial instrument and the related hedge item do not completely offset, the difference (i.e., ineffective portion of the hedge) is recognized currently in earnings.

If the hedged exposure is a cash flow exposure, the effective portion of the gains/losses on the derivative financial instrument is reported as a component of accumulated other comprehensive income and reclassified into earnings in the same period or periods during which the hedged forecasted transaction affects earnings. The ineffective portion of the gains/losses from the derivative financial instrument, if any, as well as any amounts excluded from the assessment of the cash flow hedges' effectiveness are recognized currently in other (income) expense. Effective July 2001, the Company implemented Derivatives Implementation Group Issue G20, "Cash Flow Hedges: Assessing and Measuring the Effectiveness of a Purchased Option Used in a Cash Flow Hedge," which provides guidance for assessing the effectiveness on total changes in an option's cash flows rather than only on changes in the option's intrinsic value. Time value changes were previously being recognized in current earnings since the Company excluded time value changes from its assessment of hedge effectiveness.

If the hedged exposure is a foreign currency exposure, the accounting is similar to the accounting for fair value and cash flow hedges.



## Item 1. Financial Statements (continued)

### ANADARKO PETROLEUM CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### 1. Summary of Accounting Policies (continued)

Derivative financial instruments, as well as physical delivery purchase and sale contracts, utilized in the Company's energy trading activities and in the management of price risk associated with the Company's firm transportation keep-whole commitment are accounted for under the mark-to-market accounting method pursuant to Emerging Issues Task Force Issue 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities." Under this method, the derivatives and physical delivery contracts are revalued in each accounting period and premiums and unrealized gains/losses are recorded in the statement of income and carried as assets or liabilities on the balance sheet.

The Company's derivative financial instruments associated with the marketing and trading activities are generally either exchange traded or valued by reference to a commodity that is traded in a liquid market. Valuation is determined by reference to readily available public data. Option valuations are based on the Black-Scholes option pricing model and verified against third-party quotations. The fair value of the short-term portion of the firm transportation keep-whole agreement is calculated with actively quoted natural gas basis prices, while the fair value of the long-term portion is estimated based on historical natural gas basis prices. See [Note 6](#).

**Earnings Per Share** The Company's basic earnings per share (EPS) amounts have been computed based on the average number of shares of common stock outstanding for the period. Diluted EPS amounts include the effect of the Company's outstanding stock options and performance-based stock awards under the treasury stock method and outstanding put options under the reverse treasury stock method. Diluted EPS amounts also include the net effect of the Company's convertible debentures and Zero Yield Puttable Contingent Debt Securities (ZYP-CODES) assuming the conversions occurred at the beginning of the year or the date of issuance, if later.

**New Accounting Principles** SFAS No. 143, "Accounting for Asset Retirement Obligations," requires the fair value of a liability for an asset retirement obligation to be recorded in the period in which it is incurred and a corresponding increase in the carrying amount of the related long-lived asset and will be effective for the Company in January 2003. The Company is evaluating the impact of SFAS No. 143.

SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13 and Technical Corrections," was issued in April 2002. SFAS No. 145 provides guidance for income statement classification of gains and losses on extinguishment of debt and accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. SFAS No. 145 is effective for the Company in January 2003. The Company is evaluating the impact of SFAS No. 145.

**2. Goodwill** In January 2002, the Company discontinued the amortization of goodwill in accordance with SFAS No. 142, "Goodwill and Other Intangible Assets." The transitional goodwill impairment test as of January 1, 2002 was performed and no goodwill impairment was indicated. The effects of amortization of goodwill on net income and net income per share are as follows:

<i>millions except per share amounts</i>	Three Months Ended March 31	
	2002	2001
Net income	\$ 88	\$ 656
Add: Goodwill amortization	--	17
Adjusted net income	<u>\$ 88</u>	<u>\$ 673</u>
Earnings per share - basic	\$ 0.35	\$ 2.62
Goodwill amortization per share - basic	--	0.07
Adjusted earnings per share - basic	<u>\$ 0.35</u>	<u>\$ 2.69</u>
Earnings per share - diluted	\$ 0.34	\$ 2.50
Goodwill amortization per share - diluted	--	0.07
Adjusted earnings per share - diluted	<u>\$ 0.34</u>	<u>\$ 2.57</u>

**Item 1. Financial Statements (continued)**

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**3. Inventories** The major classes of inventories, which are included in other current assets, are as follows:

<i>millions</i>	March 31, 2002	December 31, 2001
Materials and supplies	\$ 63	\$ 61
Crude oil	16	22
Natural gas	14	18
Total	<u>\$ 93</u>	<u>\$ 101</u>

**4. Properties and Equipment** Oil and gas properties include costs of \$3.57 billion at March 31, 2002 and December 31, 2001, which were excluded from capitalized costs being amortized. These amounts represent costs associated with unevaluated properties and major development projects. At March 31, 2002 and December 31, 2001, the Company's investment in countries where reserves have not been established was \$57 million and \$53 million, respectively.

Total interest costs incurred during the first quarter of 2002 and 2001 were \$87 million and \$73 million, respectively. Of these amounts, the Company capitalized \$38 million and \$51 million during the first quarter of 2002 and 2001, respectively. Capitalized interest is included as part of the cost of oil and gas properties. The interest rates for capitalization are based on the Company's weighted average cost of borrowings used to finance the expenditures applied to costs excluded that are under active evaluation.

In addition to capitalized interest, the Company also capitalized internal costs of \$43 million and \$36 million during the first quarter of 2002 and 2001, respectively. These internal costs were directly related to exploration and development activities and are included as part of the cost of oil and gas properties.

**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**5. Debt** A summary of debt follows:

<i>millions</i>	March 31, 2002		December 31, 2001	
	Principal	Carrying Value	Principal	Carrying Value
Notes Payable, Banks	\$ 266	\$ 266	\$ 228	\$ 228
Commercial Paper	229	229	226	226
Long-term Portion of Capital Lease	9	9	9	9
6.8% Debentures due 2002	88	88	88	88
6 3/4% Notes due 2003	73	73	73	73
5 7/8% Notes due 2003	83	83	83	83
6.5% Notes due 2005	170	165	170	164
7.375% Debentures due 2006	88	87	88	87
7% Notes due 2006	174	170	174	170
5 3/8% Notes due 2007	650	647	--	--
6.75% Notes due 2008	116	111	116	110
7.8% Debentures due 2008	11	11	11	11
7.3% Notes due 2009	85	82	85	82
6 3/4% Notes due 2011	950	910	950	910
6 1/8% Notes due 2012	400	395	--	--
7.05% Debentures due 2018	115	105	114	105
Zero Coupon Convertible Debentures due 2020	370	370	367	367
Zero Yield Puttable Contingent Debt Securities due 2021	30	30	650	650
7.5% Debentures due 2026	112	105	112	105
7% Debentures due 2027	54	54	54	54
6.625% Debentures due 2028	17	17	17	17
7.15% Debentures due 2028	235	212	235	212
7.20% Debentures due 2029	135	135	135	135
7.95% Debentures due 2029	117	117	117	117
7 1/2% Notes due 2031	900	862	900	862
7.73% Debentures due 2096	61	61	61	61
7 1/4% Debentures due 2096	49	49	49	49
7.5% Debentures due 2096	84	75	83	75
Total debt	<u>\$ 5,671</u>	<u>5,518</u>	<u>\$ 5,195</u>	<u>5,050</u>
Less current portion		<u>278</u>		<u>412</u>
Total long-term debt		<u>\$ 5,240</u>		<u>\$ 4,638</u>

At March 31, 2002, \$1.03 billion of notes, debentures and securities will mature or may be put to Anadarko within the next twelve months. In accordance with SFAS No. 6, "Classification of Short-term Obligations Expected to be Refinanced," \$750 million of this amount is classified as long-term debt, under the terms of Anadarko's Bank Credit Agreements. The remaining \$278 million is classified as current liabilities. At December 31, 2001, \$1.16 billion of notes, debentures and securities would mature or could be put to Anadarko within the next twelve months. In accordance with SFAS No. 6, \$750 million of this amount was classified as long-term debt, under the terms of Anadarko's Bank Credit Agreements. The remaining \$412 million was classified as current liabilities.

In March 2001, Anadarko issued \$650 million of ZYP-CODES due 2021. Holders of the ZYP-CODES have the right to require Anadarko to purchase all or a portion of their ZYP-CODES in March 2002, 2004, 2006, 2011 or 2016, at \$1,000 per ZYP-CODES. In March 2002, ZYP-CODES in the amount of \$620 million were put to the Company for repayment and were paid in cash.

## Item 1. Financial Statements (continued)

### ANADARKO PETROLEUM CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### 5. Debt (continued)

In February 2002, the Company issued \$650 million principal amount of 5 3/8% Notes due 2007. In March 2002, the Company issued \$400 million principal amount of 6 1/8% Notes due 2012. The net proceeds from these issuances were used to reduce floating rate debt and to fund a portion of the ZYP-CODES put to the Company for repayment in March 2002.

#### 6. Financial Instruments

**Commodity Derivative Financial Instruments** The Company is exposed to price risk from changing commodity prices. Management believes it is prudent to minimize the variability in cash flows on a portion of its oil and gas production. To meet this objective, the Company enters into various types of commodity derivative financial instruments to manage fluctuations in cash flows resulting from changing commodity prices. These instruments may include futures, swaps and options. Most of the instruments entered into by the Company have a term of less than one year. As of March 31, 2002, the Company had outstanding derivative financial instruments that hedged 12% of the Company's natural gas production and 18% of its crude oil production, which is expected to be produced during the remaining nine months of 2002.

Anadarko also enters into commodity derivative financial instruments (options, futures and swaps) for trading purposes with the objective of generating profits from exposure to changes in the market price of natural gas and crude oil. Commodity derivative financial instruments also provide a way to meet customers' pricing requirements while achieving a price structure consistent with the Company's overall pricing strategy. In addition, the Company uses swap agreements to reduce exposure to losses on its firm transportation keep-whole commitment with Duke Energy Field Services, Inc. (Duke). Essentially all of the derivatives used for trading purposes have a term of less than one year, with most having a term of less than three months.

Futures contracts are generally used to fix the price of expected future oil and gas sales at major industry trading locations; e.g., Henry Hub, Louisiana for gas and Cushing, Oklahoma for oil. Settlements of futures contracts are guaranteed by the New York Mercantile Exchange (NYMEX) or the International Petroleum Exchange and have nominal credit risk. Swap agreements are generally used to fix or float the price of oil and gas at the Company's market locations. Swap agreements are also used to fix the price differential between the price of gas at Henry Hub and various other market locations. Swap agreements expose the Company to credit risk to the extent the counterparty is unable to meet its monthly settlement commitment. The Company carefully monitors the creditworthiness of each counterparty. In addition, the Company routinely exercises its contractual right to net realized gains against realized losses in settling with its swap counterparties. Options are generally used to fix a floor and/or a ceiling price (a "collar") for the Company's expected future oil and gas sales. The Company buys/sells options through exchanges as well as in the over the counter market.

**Cash Flow Hedges** At March 31, 2002, the Company had option and swap contracts in place to fix floor and/or ceiling prices on a portion of expected future sales of equity gas and oil production. As of March 31, 2002, the Company had a net unrealized loss of \$26 million before taxes, or \$16 million after taxes, on derivative commodity instruments entered into to hedge equity production recorded in accumulated other comprehensive income compared to December 31, 2001, where the Company had a net unrealized gain of \$7 million before taxes (gains of \$9 million and losses of \$2 million), or \$4 million after taxes. Other income for the periods ended March 31, 2002 and 2001 included \$11 million of net losses and \$9 million of net gains, respectively, primarily due to the change in the time value of the option contracts, that was excluded from the assessment of hedge effectiveness, and the ineffective portion of the hedge. Approximately \$10 million (\$16 million before taxes) of net losses in accumulated other comprehensive income as of March 31, 2002 are expected to be reclassified into gas and oil sales during 2002 as the hedged transactions occur.

**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**6. Financial Instruments** (continued)

As of March 31, 2002 and December 31, 2001, the Company had the following volumes under derivative contracts related to its oil and gas producing activities (non-trading activity). The difference between the fair values in the table and the unrealized gain (loss) recognized in accumulated other comprehensive income is due to premiums and ineffectiveness.

**March 31, 2002**

<u>Production Period</u>	<u>Instrument Type**</u>	<u>Volumes (million MMBtu)</u>	<u>Average Price (\$ per MMBtu)</u>	<u>Net Fair Value Asset (Liability) millions</u>
<b>Natural Gas</b>				
2002	2-way collar*	1.7	3.00-5.00	\$ --
2002	3-way collar*	5.2	2.20-3.00-4.83	--
2002	Swaps*	30.6	3.09	(8)
2003	2-way collar*	2.3	3.00-5.00	--
2003	3-way collar*	6.8	2.20-3.00-4.83	(1)
2004	2-way collar*	2.3	3.00-5.00	--
2004	3-way collar*	6.9	2.20-3.00-4.83	(1)
2005	2-way collar*	2.3	3.00-5.00	--
2005	3-way collar*	6.8	2.20-3.00-4.83	(1)
2002	Calls sold	7.5	3.60	(2)
2002	Calls purchased	4.1	3.44	1
2003	Calls sold	7.4	3.15	(1)
2003	Calls purchased	10.2	3.31	1
2004	Calls sold	0.7	2.92	--
2004	Calls purchased	0.7	2.92	--
	Total			\$ (12)

<u>Production Period</u>	<u>Instrument Type**</u>	<u>Volumes (MMBbls)</u>	<u>Average Price (\$ per barrel)</u>	<u>Net Fair Value Asset (Liability) millions</u>
<b>Crude Oil</b>				
2002	Swaps*	4.3	24.58	\$ (4)
2002	2-way collar*	1.1	22.30-23.32	(3)
2002	3-way collar*	5.1	17.96-22.05-28.11	(5)
2003	Swaps*	0.8	23.80	--
2003	2-way collar*	0.4	22.30-23.32	(1)
2003	3-way collar*	3.7	17.00-21.00-26.33	(3)
	Total			\$ (16)

**Item 1. Financial Statements (continued)**

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**6. Financial Instruments (continued)**

**December 31, 2001**

<u>Production Period</u>	<u>Instrument Type**</u>	<u>Volumes (million MMBtu)</u>	<u>Average Price (\$ per MMBtu)</u>	<u>Net Fair Value Asset (Liability) millions</u>
<b>Natural Gas</b>				
2002	2-way collar*	2.3	3.00-5.00	\$ 1
2002	3-way collar*	6.8	2.20-3.00-4.83	2
2003	2-way collar*	2.3	3.00-5.00	1
2003	3-way collar*	6.8	2.20-3.00-4.83	1
2004	2-way collar*	2.3	3.00-5.00	1
2004	3-way collar*	6.9	2.20-3.00-4.83	1
2005	2-way collar*	2.3	3.00-5.00	1
2005	3-way collar*	6.8	2.20-3.00-4.83	1
2002	Calls sold	10.1	3.66	2
2002	Calls purchased	4.9	3.50	--
2003	Calls sold	7.4	3.18	(2)
2003	Calls purchased	10.2	4.12	2
2004	Calls sold	0.7	2.95	--
2004	Calls purchased	0.7	2.95	--
	Total			<u>\$ 11</u>

<u>Production Period</u>	<u>Instrument Type**</u>	<u>Volumes (MMBbls)</u>	<u>Average Price (\$ per barrel)</u>	<u>Net Fair Value Asset (Liability) millions</u>
<b>Crude Oil</b>				
2002	Swaps*	0.4	25.56	\$ 2
2002	3-way collar*	3.3	19.11-23.33-30.51	6
	Total			<u>\$ 8</u>

MMBtu – million British thermal units

MMBbls – million barrels

\* Qualifies for hedge accounting.

\*\* A "2-way collar" is a combination of options, a sold call and purchased put. The purchased put establishes a minimum price (the "floor") and the sold call establishes a maximum price (the "ceiling") the Company will receive for the volumes under contract. A "3-way collar" is a combination of options, a sold call, a purchased put and a sold put. The purchased put establishes a minimum price unless the market price falls below the sold put, at which point the minimum price would be NYMEX plus the difference between the purchased put and the sold put strike price. The sold call establishes a maximum price (the "ceiling") the Company will receive for the volumes under contract.

**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**6. Financial Instruments** (continued)

**Trading Activity** As of March 31, 2002 and December 31, 2001, the Company had the following volumes under derivative contracts related to its trading activity:

**March 31, 2002**

<u>Production Period</u>	<u>Instrument Type</u>	<u>Volumes (million MMBtu)</u>	<u>Average Price (\$ per MMBtu)</u>	<u>Net Fair Value Asset (Liability) millions</u>
<b>Natural Gas</b>				
2002	Futures sold	15.4	2.88	\$ (9)
2002	Futures purchased	16.8	3.18	5
2002	Swaps	45.6	3.31	1
2002	Calls sold	3.1	2.75	--
2002	Calls purchased	5.3	3.59	--
2002	Puts sold	6.6	3.05	(2)
2002	Puts purchased	3.5	2.54	--
2003	Futures sold	4.7	3.47	(2)
2003	Futures purchased	6.2	3.52	2
2003	Swaps	20.2	3.45	5
2004	Futures sold	0.5	3.84	--
2004	Swaps	0.2	3.89	--
2005	Swaps	1.0	3.78	--
2006	Swaps	0.6	3.69	--
	Total			\$ --

<u>Production Period</u>	<u>Instrument Type</u>	<u>Volumes (MMBbls)</u>	<u>Average Price (\$ per barrel)</u>	<u>Net Fair Value Asset (Liability) millions</u>
<b>Crude Oil</b>				
2002	Futures sold	2.1	22.44	\$ (7)
2002	Futures purchased	2.1	21.44	5
2002	Swaps	0.1	19.76	(1)
2002	Calls sold	0.3	23.50	--
2002	Calls purchased	0.2	24.00	--
2002	Puts sold	0.2	20.50	--
2002	Puts purchased	0.2	20.50	--
	Total			\$ (3)

**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**6. Financial Instruments** (continued)

**December 31, 2001**

Production Period	Instrument Type	Volumes (million MMBtu)	Average Price (\$ per MMBtu)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Natural Gas</b>				
2002	Futures sold	23.8	3.34	\$ 18
2002	Futures purchased	22.3	3.50	(21)
2002	Swaps	72.3	3.20	(42)
2002	Calls sold	8.5	3.07	1
2002	Calls purchased	12.8	4.09	1
2002	Puts sold	8.3	3.25	(7)
2002	Puts purchased	0.8	2.58	--
2003	Futures sold	1.2	3.51	--
2003	Futures purchased	0.3	3.36	--
2003	Swaps	12.2	3.12	--
	Total			<u>\$ (50)</u>

Production Period	Instrument Type	Volumes (MMBbls)	Average Price (\$ per barrel)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Crude Oil</b>				
2002	Futures sold	2.8	19.80	\$ (1)
2002	Futures purchased	1.5	20.05	2
2002	Swaps	0.5	21.77	--
2002	Calls sold	0.4	29.50	--
	Total			<u>\$ 1</u>

**Firm Transportation Keep-Whole Agreement** RME was a party to several long-term firm gas transportation agreements that supported their gas marketing program within their gathering, processing and marketing (GPM) business segment, which was sold in 1999 to Duke. Most of the GPM's firm long-term transportation contracts were transferred to Duke in the GPM disposition. One contract was retained, but is managed and operated by Duke. Anadarko is not responsible for the operations of the contracts and does not utilize the associated transportation assets to transport the Company's natural gas. As part of the GPM disposition, RME agreed to pay Duke if transportation market values fall below the fixed contract transportation rates, while Duke will pay RME if the transportation market values exceed the contract transportation rates (keep-whole agreement). Transportation contracts transferred to Duke in the GPM disposition and the contract not transferred, all of which are included in the keep-whole agreement with Duke, relate to various pipelines. This keep-whole agreement will be in effect until the earlier of each contract's expiration date or February 2009. The Company may periodically use derivative financial instruments to manage the price risk associated with this agreement. This keep-whole agreement and any oil and gas derivative financial instruments are accounted for on a mark-to-market basis. The Company recognized other expense of \$6 million and other income of \$140 million for the three months ended March 31, 2002 and 2001, respectively, related to the keep-whole agreement and associated derivative financial instruments. As of March 31, 2002 and December 31, 2001, other current assets included zero and \$25 million, other current liabilities included \$23 million and \$27 million and other long-term liabilities included \$77 million and \$80 million, respectively, related to the keep-whole agreement and associated derivative financial instruments.



**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**6. Financial Instruments** (continued)

The fair value of the short-term portion of the firm transportation keep-whole agreement is calculated with actively quoted natural gas basis prices. Basis is the difference in value between gas at various delivery points and the NYMEX gas futures contract price. Management believes that natural gas basis price quotes beyond the next twelve months are not reliable indicators of fair value due to decreasing liquidity. Accordingly, the fair value of the long-term portion is estimated based on historical natural gas basis prices, discounted at 10% per year. Management also periodically evaluates the supply and demand factors (such as expected drilling activity, anticipated pipeline construction projects, expected changes in demand at pipeline delivery points, etc.) that may impact the future market value of the firm transportation capacity to determine if the estimated fair value should be adjusted.

Anticipated discounted and undiscounted liabilities for the firm transportation keep-whole commitment at March 31, 2002 are as follows:

<i>millions</i>	March 31, 2002	
	Undiscounted	Discounted
2002	\$ 16	\$ 16
2003	23	21
2004	27	22
2005	20	15
2006	19	12
Later years	23	14
Total	<u>\$ 128</u>	<u>\$ 100</u>

As of March 31, 2002, the Company had no volumes under derivative contracts related to the firm transportation keep-whole agreement. As of December 31, 2001, the Company had the following volumes under derivative contracts related to the firm transportation keep-whole agreement:

**December 31, 2001**

Production Period	Instrument Type	Volumes (million MMBtu)*	Average Price (\$ per MMBtu)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Natural Gas</b>				
2002	Swaps	4.2	8.42	\$ 25

\* Represents 2% of the Company's total volumetric exposure under the keep-whole agreement for 2002.

**7. Preferred Stock** For the first quarter of 2002 and 2001, dividends of \$13.65 per share (equivalent to \$1.365 per Depositary Share) were paid to holders of preferred stock.

**Item 1. Financial Statements (continued)**

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**8. Common Stock** The Company's credit agreements allow for a maximum capitalization ratio of 60% debt, exclusive of the effect of any non-cash writedowns. While there is no specific restriction on paying dividends, under the maximum debt capitalization ratio retained earnings were not restricted as to the payment of dividends at March 31, 2002 and December 31, 2001.

The reconciliation between basic and diluted EPS is as follows:

<i>millions except per share amounts</i>	Three Months Ended March 31, 2002			Three Months Ended March 31, 2001		
	<u>Income</u>	<u>Shares</u>	<u>Per Share Amount</u>	<u>Income</u>	<u>Shares</u>	<u>Per Share Amount</u>
<b>Basic EPS</b>						
Net income available to common stockholders before change in accounting principle	\$ 88	248	\$ <u>0.35</u>	\$ 661	250	\$ <u>2.64</u>
Effect of convertible debentures and ZYP-CODES	2	13		2	10	
Effect of dilutive stock options and performance-based stock awards	<u>--</u>	<u>2</u>		<u>--</u>	<u>3</u>	
<b>Diluted EPS</b>						
Net income available to common stockholders plus assumed conversion	\$ <u>90</u>	<u>263</u>	\$ <u>0.34</u>	\$ <u>663</u>	<u>263</u>	\$ <u>2.52</u>

For the three months ended March 31, 2002 and 2001, options for 1.4 million and 0.1 million shares, respectively, of common stock were excluded from the diluted EPS calculation because the options' exercise price was greater than the average market price of common stock for the period. For the three months ended March 31, 2002, put options for 1 million shares of common stock were excluded because the put options' exercise price was less than the average market price of common stock for the period.

In 2001, the Board of Directors authorized the Company to purchase up to \$1 billion in shares of Anadarko common stock. The share purchases may be made from time to time, depending on market conditions. Shares may be purchased either in the open market or through privately negotiated transactions. The repurchase program does not obligate Anadarko to acquire any specific number of shares and may be discontinued at any time. During 2001, the Company purchased 2.2 million shares of common stock for \$116 million. In January 2002, the Company purchased an additional 1 million shares of common stock for \$50 million.

To enhance the share repurchase program, Anadarko has sold put options to independent third parties. These put options entitle the holder to sell shares of Anadarko common stock to the Company on certain dates at specified prices. During 2001, Anadarko sold put options for the purchase of a total of 5 million shares of Anadarko common stock with a notional amount of \$240 million. Put options for 1 million shares were exercised and put options for 2 million shares expired unexercised in 2001. In January 2002, the Company entered into an additional put option for 1 million shares of Anadarko common stock with a notional amount of \$46 million and received a \$3 million premium. Put options for an additional 2 million shares expired unexercised in 2002. The remaining put option for 1 million shares will expire in July 2002, if not exercised. The put option permits a net-share settlement at the Company's option and does not result in a liability on the consolidated balance sheet as of March 31, 2002.

**Item 1. Financial Statements (continued)**

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**9. Statement of Cash Flows Supplemental Information** The amounts of cash paid (received) for interest (net of amounts capitalized) and income taxes are as follows:

	Three Months Ended March 31	
<i>millions</i>	2002	2001
Interest	\$ 10	\$ 13
Income taxes	\$ (7)	\$ 112

**10. Segment Information** The following table illustrates information related to Anadarko's business segments. The segment shown as All Other includes smaller operating units, corporate activities, financing activities and inter-company eliminations.

<i>millions</i>	Oil and Gas Exploration and Production	Marketing	Minerals	All Other	Total
<b>Three Months Ended March 31:</b>					
<b>2002</b>					
Revenues	\$ 608	\$ 744	\$ 13	\$ 8	\$ 1,373
Intersegment revenues	137	2	--	(139)	--
Total revenues	745	746	13	(131)	1,373
Income (loss) before income taxes	\$ 255	\$ (14)	\$ 11	\$ (120)	\$ 132
Net properties and equipment	\$ 12,314	\$ 246	\$ 1,205	\$ 400	\$ 14,165
Goodwill	\$ 1,432	\$ --	\$ --	\$ --	\$ 1,432
<b>2001</b>					
Revenues	\$ 1,064	\$ 1,942	\$ 11	\$ (8)	\$ 3,009
Intersegment revenues	484	11	--	(495)	--
Total revenues	1,548	1,953	11	(503)	3,009
Income (loss) before income taxes	\$ 1,032	\$ 154	\$ 10	\$ (143)	\$ 1,053
Net properties and equipment	\$ 12,773	\$ 185	\$ 1,210	\$ 303	\$ 14,471
Goodwill	\$ 1,524	\$ --	\$ --	\$ --	\$ 1,524

**11. Other (Income) Expense** Other (income) expense consists of the following:

	Three Months Ended March 31	
<i>millions</i>	2002	2001
Firm transportation keep-whole contract valuation (See <a href="#">Note 6</a> )	\$ 6	\$ (140)
Foreign currency exchange *	(1)	52
Corporate hedge ineffectiveness and change in time value	11	(9)
Other	7	1
Total	\$ 23	\$ (96)

\* 2002 excludes \$13 million in transaction gains related to remeasurement of the Venezuela deferred tax liability, which is included in income tax expense.

## Item 1. Financial Statements (continued)

### ANADARKO PETROLEUM CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### 12. Commitments

**Synthetic Leases** In November 1999, Anadarko entered into a build-to-suit lease arrangement for its corporate office building in The Woodlands, Texas. The development and acquisition of the property was financed by a special purpose entity (SPE) sponsored by a financial institution. The lease balance to be funded under this arrangement will not exceed \$185 million. The SPE is not consolidated in the Company's financial statements and, based on the initial terms of the agreement, the Company has accounted for this arrangement as an operating lease in accordance with SFAS No. 13, "Accounting for Leases."

The initial lease term is five years, with up to seven one-year renewal options. Monthly lease payments are based on the London interbank borrowing rate applied against the lease balance and will begin in 2002. The lease contains various covenants including covenants regarding the Company's financial condition. Default under the lease, including violation of these covenants, could require the Company to purchase the facility for a specified amount, which approximates the lessor's original cost (\$143 million funded as of March 31, 2002). As of March 31, 2002, the Company was in compliance with these covenants.

At the end of the lease term, the Company has an option to either purchase the facility for the purchase option amount of the lease balance plus any outstanding lease payments or to assist the SPE in the sale of the property. The Company has provided a residual value guarantee for any deficiency if the property is sold for less than the sale option amount (\$120 million at March 31, 2002). In addition, the Company is entitled to any proceeds from a sale of the property in excess of the purchase option amount.

In December 2000, the Company entered into a lease arrangement for an office building in The Woodlands, Texas. The acquisition of the property was financed by an SPE sponsored by a financial institution. The amount funded was \$48 million. The SPE is not consolidated in the Company's financial statements and the Company has accounted for this arrangement as an operating lease in accordance with SFAS No. 13.

The initial lease term is five years. Monthly lease payments, which began in 2001, are based on the London interbank borrowing rate applied against the \$48 million lease balance. The lease contains various covenants including covenants regarding the Company's financial condition. Default under the lease, including violation of these covenants, could require the Company to purchase the facility for a specified amount, which approximates the lessor's original cost (\$48 million). As of March 31, 2002, the Company is in compliance with these covenants.

At the end of the lease term, the Company has an option to either purchase the facility for the purchase option amount of \$48 million plus any outstanding lease payments or to assist the SPE in the sale of the property. The Company has provided a residual value guarantee for any deficiency if the property is sold for less than the sale option amount (\$39 million at March 31, 2002). In addition, the Company is entitled to any proceeds from a sale of the property in excess of the purchase option amount.

If for either of these leases, the Company determines that it is probable that the expected fair value of the property at the end of the lease term will be less than the purchase option amount, the Company will accrue the expected loss on a straight line basis over the remaining lease term. Currently, management does not believe it is probable that the fair market value of either of these properties will be less than the purchase option amount at the end of the lease term.

**Production Platform** In April 2002, the Company signed an agreement under which a floating production platform for its Marco Polo discovery in Green Canyon Block 608 of the Gulf of Mexico will be installed. The other partners will construct the platform and processing facilities that upon completion, expected in 2004, will be operated by Anadarko. The agreement provides that Anadarko will dedicate its production from Green Canyon Block 608 and 11 other Green Canyon blocks to the processing facilities. The agreement will require a monthly demand charge of slightly

## Item 1. Financial Statements (continued)

### ANADARKO PETROLEUM CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### 12. Commitments (continued)

over \$2 million for five years beginning at the time of project completion and a processing fee based upon production. Anadarko will be entitled to 25% of the net after tax cash proceeds from these facilities after payout, as defined, is attained. The agreement does not contain any purchase options, purchase obligations or value guarantees.

#### 13. Contingencies

**General** The Company is a defendant in a number of lawsuits and is involved in governmental proceedings arising in the ordinary course of business, including, but not limited to, royalty claims, contract claims and environmental claims. The Company has also been named as a defendant in various personal injury claims, including numerous claims by employees of third-party contractors alleging exposure to asbestos and benzene while working at a refinery in Corpus Christi, Texas, which RME sold in segments in 1987 and 1989. While the ultimate outcome and impact on the Company cannot be predicted with certainty, management believes that the resolution of these proceedings will not have a material adverse effect on the consolidated financial position of the Company, although results of operations and cash flow could be significantly impacted in the reporting periods in which such matters are resolved. Discussed below are several specific proceedings.

**Superfund** Presently, five Superfund sites (four Federal and one State) are included in the Superfund Reserve.

**Operating Industries, Inc. (Federal)** - The former municipal industrial landfill, located in Monterey Park, California, was operational between 1948 and 1984. RME was noticed as a Potentially Responsible Party (PRP) in June 1986 for its Wilmington Production Field's and Wilmington Refinery's contributions. The Company has agreed to participate in a settlement with the Environmental Protection Agency (EPA). The Company's estimated share of this settlement is \$5.1 million. The settlement and consent decree are undergoing final agency review.

**Ekotek (Federal)** - The facility in Salt Lake City, Utah operated as a refinery from 1953 until 1978, at which time it was converted to a hazardous waste storage/treatment and petroleum recycling facility. The Utah Department of Environmental Quality issued multiple Notices of Violation to the facility in 1988, resulting in the facility's closing. Bear Creek Uranium Company, an affiliate, was named as a PRP for its contributions of used/waste oils. Remediation of the Ekotek site is nearing completion and no additional funding requests are expected.

**Casmalia (Federal)** - The Casmalia facility, located in Santa Barbara County, California, is a former Resource Conservation and Recovery Act hazardous waste disposal site. RME was noticed as a PRP in March 1993. RME's waste contribution is attributed to the Wilmington Refinery. Negotiations with the EPA are ongoing. The Company believes its share of the costs will be about \$0.1 million.

**Geothermal Inc. (State)** - The site, located in Middletown, California, was permitted as a Class II surface impoundment facility for geothermal wastes. Sludge from drilling operations and power plant wastes generated at the Geysers Geothermal Field between 1976 and 1987 were transported to the facility for treatment/disposal. The waste material was placed in evaporation ponds and allowed to dry. The resultant solids were buried onsite. Site remediation began in 1984. Anadarko was noticed as a PRP in December 1993. Several remedial methods are currently being evaluated to determine the most effective for addressing site groundwater impacts. The Company believes its share of the costs will be about \$0.1 million.

**PCB Treatment, Inc. (Federal)** - The PCB treatment/disposal site, located in Kansas City, Kansas and Kansas City, Missouri, operated from 1982 until 1986 when regulatory violations forced its closure. RME was noticed as a PRP in October 1998 for contributions attributed to Wilmington Refinery operations. PCB impacts are currently limited to the facility structures and surrounding soils. Remedial alternatives are under review. The Company believes its share of the costs will be about \$0.1 million.

## Item 1. Financial Statements (continued)

### ANADARKO PETROLEUM CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### 13. Contingencies (continued)

**Royalty Litigation** During September 2000, the Company was named as a defendant in a case styled *U.S. of America ex rel. Harold E. Wright v. AGIP Company, et al.* (the "Gas Qui Tam case") filed in the U.S. District Court for the Eastern District of Texas, Lufkin Division. This lawsuit generally alleges that the Company and 118 other defendants improperly measured and otherwise undervalued natural gas in connection with a payment of royalties on production from federal and Indian lands. The case has been transferred to the U.S. District Court, Multi-District Litigation Docket pending in Wyoming. Based on the Company's present understanding of the various governmental and False Claims Act proceedings described above, the Company believes that it has substantial defenses to these claims and intends to vigorously assert such defenses. However, if the Company is found to have violated the Civil False Claims Act, the Company could be subject to a variety of sanctions, including treble damages and substantial monetary fines.

A group of royalty owners purporting to represent RME's gas royalty owners in Texas (*Neinast, et al.*) was granted class action certification in December 1999, by the 21st Judicial District Court of Washington County, Texas, in connection with a gas royalty underpayment case against the Company. This certification did not constitute a review by the Court of the merits of the claims being asserted. The royalty owners' pleadings did not specify the damages being claimed, although most recently a demand for damages in the amount of \$100 million has been asserted. The Company is of the opinion that the amount of damages at risk is substantially less than the amount demanded by the class action counsel and the Company intends to vigorously assert its defenses. The Company appealed the class certification order. A favorable decision from the Houston Court of Appeals decertified the class. The royalty owners have not appealed this matter to the Texas Supreme Court and the decision from the Houston Court of Appeals will become final.

A class action lawsuit entitled *Gilbert H. Coulter, et al. v. Anadarko Petroleum Corporation* has been certified in the 26th Judicial District Court, Stevens County, Kansas. In this action, the royalty owners contend that royalty was underpaid as a result of the deduction for certain post-production costs in the calculation of royalty. The Company believes that its method of calculating royalty was proper and that its gas was marketable in the condition produced, and thus plaintiffs' claims are without merit. This case was certified as a class action in August 2000 and was tried in February 2002. A decision from the trial court is expected by the end of 2002.

**Citgo Litigation** CITGO Petroleum Corporation's (CITGO) claims arise out of an Asset Purchase and Contribution Agreement dated March 17, 1987 whereby RME's predecessor sold a refinery located in Corpus Christi, Texas, to CITGO's predecessor. After the sale of the refinery, numerous individuals living near the refinery sued CITGO (the Neighborhood Litigation) thereby implicating the Asset Purchase and Contribution Agreement indemnity provision. CITGO and RME eventually entered into a settlement agreement to allocate, on an interim basis, each party's liability for defense and liability cost in that and related litigation. That agreement provides that once the Neighborhood Litigation and certain related claims are resolved, then the parties will determine their final indemnity obligations to each other through binding arbitration. At the present time, RME and CITGO have agreed to defer arbitrating the allocation of responsibility for this liability in order to focus their efforts on a global settlement. Arbitration will resume upon request of either CITGO or RME. In conjunction with this matter, RME sued Continental Insurance for denial of coverage for claims related to this dispute. RME and Continental Insurance settled the insurance coverage litigation which resulted in Continental Insurance paying RME for the claims. Negotiations and discussions with CITGO continue.

#### Kansas Ad Valorem Tax

**General** The Natural Gas Policy Act of 1978 allowed a "severance, production or similar" tax to be included as an add-on, over and above the maximum lawful price for natural gas. Based on the Federal Energy Regulatory Commission (FERC) ruling that the Kansas ad valorem tax was such a tax, the Company collected the Kansas ad valorem tax.

## Item 1. Financial Statements (continued)

### ANADARKO PETROLEUM CORPORATION NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

#### 13. Contingencies (continued)

*Background of PanEnergy Litigation* FERC's ruling regarding the ability of producers to collect the Kansas ad valorem tax was appealed to the United States Court of Appeals for the District of Columbia Circuit (D.C. Circuit). The Court held in June 1988 that FERC failed to provide a reasoned basis for its findings and remanded the case to FERC.

Ultimately, the D.C. Circuit issued a decision on August 2, 1996 ruling that producers must refund all Kansas ad valorem taxes collected relating to production since October 1983. The Company filed a petition for writ of certiorari with the Supreme Court. That petition was denied on May 12, 1997.

*PanEnergy Litigation* On May 13, 1997, the Company filed a lawsuit in the Federal District Court for the Southern District of Texas against PanEnergy seeking declaration that pursuant to prior agreements Anadarko is not required to issue refunds to PanEnergy for the principal amount of \$14 million (before taxes) and, if the petition for adjustment is denied in its entirety by FERC with respect to PanEnergy refunds, interest in an amount of \$38 million (before taxes). The Company also sought from PanEnergy the return of the \$1 million (before taxes) charged against income in 1993 and 1994. In October 2000, the U.S. Magistrate issued recommendations concerning motions for summary judgment previously filed by both parties. In essence, the Magistrate's recommendation finds that the Company should be responsible for refunds attributable to the time period following August 1, 1985 while Duke Energy (as the successor company to Anadarko Production Company) should be responsible for refunds attributable to the time period before August 1, 1985.

The Company reached a settlement agreement with PanEnergy that required the Company to pay \$15 million for settlement in full of all matters relating to the refunds of Kansas ad valorem tax reimbursements collected by the Company as first seller from August 1, 1985 through 1988. The settlement agreement was approved by the FERC and paid by Anadarko during 2001. The settlement agreement does not have any impact on the outstanding dispute between the Company and PanEnergy in connection with the refunds that relate to the Cimmaron River System. Anadarko's net income for 2001 included a \$15 million charge (before taxes) related to the settlement agreement. Discussions with the Kansas Corporation Commission and PanEnergy to reach a settlement of the Cimmaron River System dispute are ongoing. At this time, it is estimated that a resolution may be reached in the first half of 2002, that may result in a payment by the Company of about \$7 million. Accordingly, a provision for \$7 million was charged against income in 2001.

*Other Litigation* The Company has a reserve of \$8 million for Kansas ad valorem tax refunds of RME. This amount reflects all principal and interest that may be due at the conclusion of all regulatory proceedings and litigation to parties other than PanEnergy.

**Lease Agreement** The Company, through one of its affiliates, is a party to a lease agreement (base lease) for the leveraged lease financing of the Corpus Christi West Plant Refinery (West Plant) with an initial term expiring December 31, 2003, and successive renewal periods lasting through January 31, 2011. At the conclusion of the initial term of the base lease, any renewal period or January 31, 2011, the Company has the right to purchase the West Plant at the fair market sales value. In connection with the sale by RME of its refining business in 1987 and 1989, the West Plant was subleased to CITGO with sublease payments during the initial term equal to the Company's base lease payments and during any renewal period equal to the lesser of the base lease rental, which will be tied to the annual fair market rental value or a specified maximum amount. Additionally, CITGO has the option under the sublease to purchase the West Plant from the Company at the conclusion of the initial term or any renewal term at the fair market sales value, or on January 31, 2011 at a nominal price. If the fair market rental value of the base lease during any renewal term exceeds CITGO's maximum obligation under the sublease, or if CITGO purchases the West Plant on January 31, 2011 and the fair market sales value of the West Plant is greater than the purchase amount specified in the sublease, the Company will be obligated to pay the excess amounts. The Company is unable at this time to determine the fair market rental value or the fair market sales value of the West Plant, but will at least annually evaluate the potential effect of the obligation.

**Item 1. Financial Statements** (continued)

**ANADARKO PETROLEUM CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**13. Contingencies** (continued)

**Guarantees** Anadarko is guarantor for certain obligations of its wholly-owned and consolidated subsidiaries, which are included in the consolidated financial statements and notes. In addition, the Company is guarantor for specific financial obligations of two trona mining affiliates. The investments in these entities, which are not consolidated subsidiaries, are accounted for using the equity method. The Company has guaranteed a portion of certain Industrial Revenue Bonds, amounts due under a revolving credit agreement and letters of credit required for environmental surety bonds. The amount the Company would be obligated to pay should the affiliates default on these obligations would be up to \$8 million for environmental surety bonds and \$38 million for debt.

**Other** In connection with a sale of properties, the Company has agreed to indemnify the purchaser for the use of certain currency remeasurement losses claimed by the Company in previously filed tax returns, which are currently being evaluated by the taxing authorities. The Company believes it is probable that these losses will be disallowed and will have to be settled with the purchaser in cash. The Company has a \$22 million liability recorded for the contingency.



## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

*The Company has made in this report, and may from time to time otherwise make in other public filings, press releases and discussions with Company management, forward looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 concerning the Company's operations, economic performance and financial condition. These forward looking statements include information concerning future production and reserves, schedules, plans, timing of development, contributions from oil and gas properties, and those statements preceded by, followed by or that otherwise include the words "believes", "expects", "anticipates", "intends", "estimates", "projects", "target", "goal", "plans", "objective", "should" or similar expressions or variations on such expressions. For such statements, the Company claims the protection of the safe harbor for forward looking statements contained in the Private Securities Litigation Reform Act of 1995. Such statements are subject to various risks and uncertainties, and actual results could differ materially from those expressed or implied by such statements due to a number of factors in addition to those discussed elsewhere in this Form 10-Q and in the Company's other public filings, press releases and discussions with Company management. Anadarko undertakes no obligation to publicly update or revise any forward looking statements. See "Regulatory Matters and Additional Factors Affecting Business" and "Critical Accounting Policies" in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in the Company's 2001 Annual Report on Form 10-K.*

### Financial Results

#### Selected Financial Data

<i>millions except per share amounts</i>	Three Months Ended March 31	
	2002	2001
Revenues	\$ 1,373	\$ 3,009
Costs and expenses	1,169	2,020
Merger expenses	--	10
Interest expense	49	22
Other (income) expense	23	(96)
Income taxes	43	389
Net income available to common stockholders before cumulative effect of change in accounting principle	\$ 88	\$ 661
Net income available to common stockholders	\$ 88	\$ 656
Earnings per share - before cumulative effect of change in accounting principle - basic	\$ 0.35	\$ 2.64
Earnings per share - before cumulative effect of change in accounting principle - diluted	\$ 0.34	\$ 2.52
Earnings per share - basic	\$ 0.35	\$ 2.62
Earnings per share - diluted	\$ 0.34	\$ 2.50

**Net Income** Anadarko's net income available to common stockholders in the first quarter of 2002 totaled \$88 million or \$0.34 per share (diluted) compared to net income of \$656 million or \$2.50 per share (diluted) for the first quarter of 2001. Net income for the first quarter of 2002 and 2001 includes charges of \$8 million (\$5 million after taxes) and \$7 million (\$4 million after taxes), respectively, for impairments related to international oil and gas properties. The Company's net income available to common stockholders excluding the impairments was \$93 million or \$0.36 per share (diluted) for the first quarter 2002 compared to \$660 million or \$2.52 per share (diluted) for the same period of 2001.

In January 2002, the Company discontinued the amortization of goodwill in accordance with Statement of Financial Accounting Standards (SFAS) No. 142, "Goodwill and Other Intangible Assets." Stated without amortization of goodwill, net income available to common stockholders for the first quarter of 2001 would have been \$673 million or \$2.57 per share (diluted).

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****Revenues**

<i>millions</i>	Three Months Ended March 31	
	2002	2001
Gas sales	\$ 353	\$ 1,114
Oil and condensate sales	350	361
Natural gas liquids sales	42	73
Marketing sales	607	1,458
Minerals and other	21	3
Total	<u>\$ 1,373</u>	<u>\$ 3,009</u>

Total revenues for the first quarter 2002 decreased \$1.64 billion or 54% compared to the first quarter of 2001. Natural gas, crude oil and condensate and natural gas liquids (NGLs) revenues for the first quarter of 2002 decreased \$803 million or 52% to \$745 million compared to \$1.55 billion for the first quarter of 2001, due primarily to a significant decrease in natural gas prices, as well as decreases in crude oil, condensate and NGLs prices. Marketing sales for the first quarter of 2002 decreased \$851 million or 58% compared to the same period of 2001. The decrease in marketing sales, which is due primarily to decreases in commodity prices, is partially offset by a decrease in marketing purchases of \$837 million.

**Analysis of Oil and Gas Sales Volumes**

<b>Barrels of Oil Equivalent (MMBOE)</b>	Three Months Ended March 31	
	2002	2001
United States	35	34
Canada	8	7
Algeria	5	2
Other International	<u>2</u>	<u>4</u>
Total	<u>50</u>	<u>47</u>

MMBOE - million barrels of oil equivalent

During the first quarter of 2002, Anadarko sold 50 MMBOE, an increase of 3 MMBOE or 6% compared to sales of 47 MMBOE in the first quarter of 2001. The increase in volumes during 2002 was due primarily to an increase of 3 MMBOE from operations in Algeria due to the expansion of production facilities in late 2001, an increase of 1 MMBOE from the Berkley Petroleum Corp. (Berkley) acquisition in 2001 and an increase of 1 MMBOE in the United States, primarily from Alaska. These increases were partially offset by a decrease of 2 MMBOE related to the disposition of operations in Guatemala and Argentina in 2001. Sales volumes represent actual production volumes adjusted for changes in commodity inventories. Anadarko employs marketing strategies to help manage production and sales volumes and mitigate the effect of price volatility, which is likely to continue in the future. See [Derivative Financial Instruments](#) under Item 3 of this Form 10-Q.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

**Natural Gas Sales Volumes and Average Prices**

	Three Months Ended March 31	
	2002	2001
<b>United States (Bcf)</b>	131	139
MMcf/d	1,458	1,548
Price per Mcf before hedge	\$ 2.13	\$ 6.81
Effect of hedge per Mcf	--	0.05
Price per Mcf	<u>\$ 2.13</u>	<u>\$ 6.86</u>
<b>Canada (Bcf)</b>	31	24
MMcf/d	347	269
Price per Mcf before hedge	\$ 2.47	\$ 6.44
Effect of hedge per Mcf	(0.13)	0.06
Price per Mcf	<u>\$ 2.34</u>	<u>\$ 6.50</u>
<b>Other International (Bcf)</b>	--	1
MMcf/d	--	5
Price per Mcf	<u>--</u>	<u>\$ 1.03</u>
<b>Total (Bcf)</b>	162	164
MMcf/d	1,805	1,822
Price per Mcf before hedge	\$ 2.19	\$ 6.74
Effect of hedge per Mcf	(0.02)	0.05
Price per Mcf	<u>\$ 2.17</u>	<u>\$ 6.79</u>

Bcf - billion cubic feet

Mcf - thousand cubic feet

MMcf/d - million cubic feet per day

The Company's natural gas sales volumes for the first quarter 2002 were down 2 Bcf or 1% compared to the first quarter of 2001. The decrease in volumes is due primarily to a slight decrease in the Company's sales volumes within the U.S. as a result of reduced spending for development drilling, a strategy the Company adopted in the third quarter of 2001 in response to lower commodity prices. This decrease is partially offset by an increase in volumes from Canada due to the Berkley acquisition in 2001. Production of natural gas is generally not directly affected by seasonal swings in demand. However, the Company may decide during periods of low commodity prices to decrease development activity, which can result in decreased production volumes.

The Company's average wellhead gas price in the first quarter of 2002 decreased 68% from the first quarter of 2001. The decrease in prices during 2002 was attributed to a severe decline in natural gas demand as a result of high prices in early 2001, a national economic downturn and mild summer weather in 2001. The Company hedged only 12% of its remaining forecasted 2002 natural gas wellhead sales volumes as of March 31, 2002. As a result, future natural gas revenues are subject to continued volatility based on fluctuations in market prices.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)**

**Crude Oil and Condensate Sales Volumes and Average Prices**

	Three Months Ended March 31	
	2002	2001
<b>United States (MMBbls)</b>	9	8
MBbls/d	91	89
Price per barrel before hedge	\$ 18.76	\$ 25.52
Effect of hedge per barrel	<u>0.24</u>	<u>(0.08)</u>
Price per barrel	<u>\$ 19.00</u>	<u>\$ 25.44</u>
<b>Canada (MMBbls)</b>	3	3
MBbls/d	38	31
Price per barrel before hedge	\$ 15.77	\$ 16.24
Effect of hedge per barrel	<u>0.16</u>	<u>0.32</u>
Price per barrel	<u>\$ 15.93</u>	<u>\$ 16.56</u>
<b>Algeria (MMBbls)</b>	5	2
MBbls/d	59	25
Price per barrel	<u>\$ 20.12</u>	<u>\$ 25.12</u>
<b>Other International (MMBbls)</b>	2	4
MBbls/d	24	41
Price per barrel	<u>\$ 15.38</u>	<u>\$ 14.87</u>
<b>Total (MMBbls)</b>	19	17
MBbls/d	212	186
Price per barrel before hedge	\$ 18.22	\$ 21.57
Effect of hedge per barrel	<u>0.14</u>	<u>0.02</u>
Price per barrel	<u>\$ 18.36</u>	<u>\$ 21.59</u>

MMBbls - million barrels

MBbls/d - thousand barrels per day

Anadarko's crude oil and condensate sales volumes for the first three months of 2002 increased 2 MMBbls or 12% compared to the first three months of 2001. The increase in crude oil and condensate sales volumes was due primarily to an increase of approximately 3 MMBbls from operations in Algeria related to the expansion of production facilities in late 2001 and an increase of 1 MMBbls from operations in the United States, primarily from Alaska. These increases were partially offset by a decrease of 2 MMBbls related to the sale of producing properties in Guatemala and Argentina during 2001. Production of oil usually is not affected by seasonal swings in demand or in market prices.

Anadarko's average realized crude oil prices for the first quarter of 2002 decreased 15% compared to the first quarter of 2001. The decrease in crude oil prices during 2002 is attributed primarily to a modest increase in supply and very slow growth in demand due to a worldwide economic downturn and a sharp decline in jet fuel consumption. The Company hedged only 18% of its remaining forecasted 2002 crude oil wellhead sales volumes as of March 31, 2002. As a result, future oil and condensate revenues are subject to continued volatility based on fluctuations in market prices.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****Natural Gas Liquids Sales Volumes and Average Prices**

	Three Months Ended March 31	
	2002	2001
<b>Total (MMBbls)</b>	4	3
MBbls/d	40	36
Price per barrel	\$ 11.61	\$ 22.54

The Company's NGLs sales volumes in the first quarter of 2002 increased 33% compared to the first quarter of 2001. During the first quarter of 2002, average NGLs prices declined 48% compared to the first quarter of 2001.

**Costs and Expenses**

<i>millions</i>	Three Months Ended March 31	
	2002	2001
Marketing purchases	\$ 596	\$ 1,433
Operating expenses	170	157
Administrative and general	72	49
Depreciation, depletion and amortization	267	274
Other taxes	56	83
Impairments related to oil and gas properties	8	7
Amortization of goodwill	--	17
<b>Total</b>	<b>\$ 1,169</b>	<b>\$ 2,020</b>

During the first quarter of 2002, Anadarko's costs and expenses decreased \$851 million or 42% compared to the first quarter of 2001 due to the following factors:

- Marketing purchases decreased \$837 million (58%) due primarily to decreases in prices for gas and oil volumes purchased from third parties.
- Operating expenses increased \$13 million (8%) primarily due to an increase in oil field service costs and production volumes.
- Administrative and general expenses increased \$23 million (47%) primarily due to increases in salaries and benefits expenses associated with the Company's workforce.
- Depreciation, depletion and amortization (DD&A) expense decreased \$7 million (3%). The decrease is due primarily to a lower DD&A rate for oil and gas properties in 2002 as a result of ceiling test impairments in the third quarter of 2001. This decrease is partially offset by an increase in DD&A related to higher production volumes in 2002.
- Other taxes decreased \$27 million (33%) primarily due to a decrease in production taxes related to the significantly lower commodity prices in 2002.
- Impairments of oil and gas properties were primarily due to unsuccessful exploration activities in Australia in 2002 and Ghana in 2001.
- Amortization of goodwill decreased \$17 million due to discontinuing amortization of goodwill in 2002 in accordance with SFAS No. 142.

**Merger Expenses**

During the first quarter of 2001, merger costs of \$10 million were expensed related to mergers and acquisitions that took place in 2000 and 2001. These costs related primarily to transition, integration, hiring and relocation costs, vesting of restricted stock and stock options, and retention bonuses. Any additional expenses related to these acquisitions are expected to be minimal and are included in administrative and general expenses.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)****Interest Expense**

<i>millions</i>	Three Months Ended March 31	
	2002	2001
Gross interest expense	\$ 87	\$ 73
Capitalized interest	<u>(38)</u>	<u>(51)</u>
Net interest expense	<u>\$ 49</u>	<u>\$ 22</u>

Gross interest expense in the first quarter of 2002 increased 19% compared to the first quarter of 2001. The increase is due to higher average debt outstanding in 2002 compared to 2001 primarily because of acquisitions in 2001 and capital spending. See [Capital Resources and Liquidity](#) and [Outlook on Liquidity](#).

For the first three months of 2002, capitalized interest decreased by 25% compared to the same period of 2001 primarily due to a decrease in capitalized costs that qualify for interest capitalization.

**Other (Income) Expense**

<i>millions</i>	Three Months Ended March 31	
	2002	2001
Firm transportation keep-whole contract valuation	\$ 6	\$ (140)
Foreign currency exchange	(1)	52
Corporate hedge ineffectiveness and change in time value	11	(9)
Other	<u>7</u>	<u>1</u>
Total	<u>\$ 23</u>	<u>\$ (96)</u>

Other income in the first quarter of 2002 decreased \$119 million compared to the same period of 2001 due primarily to a \$146 million decrease related to the effect of significantly lower market value for firm transportation subject to a keep-whole agreement and a \$20 million decrease related to losses on corporate hedges, partially offset by a \$53 million decrease in foreign currency exchange losses primarily due to the restructuring of Canadian debt and changes in the Canadian exchange rate. See [Derivative Financial Instruments](#) and [Foreign Currency Risk](#) under Item 3 of this Form 10-Q.

**Income Taxes**

<i>millions</i>	Three Months Ended March 31	
	2002	2001
Income taxes	\$ 43	\$ 389

For the first quarter of 2002, income taxes decreased \$346 million or 89% compared to \$389 million for the first quarter of 2001. The decrease was due primarily to the decrease in earnings before income taxes and \$13 million in transaction gains related to remeasurement of the Venezuela deferred tax liability.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

### Marketing Strategies

**Overview** The Company's sales of natural gas, crude oil, condensate and NGLs are generally made at the market prices of those products at the time of sale. Therefore, even though the Company has several large purchasers, the Company believes other purchasers would be willing to buy the Company's natural gas, crude oil, condensate and NGLs at comparable market prices. The Company's marketing department actively manages sales of its oil and gas through Anadarko Energy Services Company, Anadarko, Anadarko Canada Corporation and RME Holding Company (RME). The Company also conducts trading activities for the purpose of generating profits on or from exposure to changes in the market prices of gas, crude oil, condensate and NGLs. However, the Company does not engage in market-making practices nor does it trade in any non-energy-related commodities. The Company's trading risk position, most of the time, is a net short position that is offset by the Company's natural long position as a producer. Essentially all of the Company's trading transactions have a term of less than one year and most are less than three months. See [Derivative Financial Instruments](#) under Item 3 of this Form 10-Q.

**Marketing Contracts** The following schedules provide additional information regarding the Company's marketing and trading portfolio of physical and derivative contracts and the firm transportation keep-whole agreement as of March 31, 2002. The Company records income on these activities using the mark-to-market method. In the first quarter of 2002, the use of mark-to-market accounting compared to historical cost accounting resulted in reduced non-cash income of \$27 million, before taxes, related to the marketing and trading activities and reduced non-cash income related to the firm transportation keep-whole agreement of \$17 million, before taxes. In the first quarter of 2001, the use of mark-to-market accounting compared to historical cost accounting resulted in additional non-cash income of \$17 million, before taxes, related to the marketing and trading activities and \$80 million, before taxes, related to the firm transportation keep-whole agreement.

<i>millions</i>	Marketing and Trading	Firm Transportation Keep-whole	Total
Fair value of contracts outstanding at December 31, 2001	\$ 17	\$ (82)	\$ (65)
Contracts realized or otherwise settled during period	(5)	(12)	(17)
Fair value of new contracts when entered into during period	1	--	1
Other changes in fair value	(21)	(6)	(27)
Fair value of contracts outstanding at March 31, 2002	\$ (8)	\$ (100)	\$ (108)

<b>Assets (Liabilities)</b> <i>millions</i>	Fair Value of Contracts at March 31, 2002				
	Matures 2002	Matures 2003- 2004	Matures 2005- 2006	Matures Thereafter	Total
<b>Marketing and Trading</b>					
Prices actively quoted	\$ (7)	\$ (1)	\$ --	\$ --	\$ (8)
Prices based on models and other valuation methods	--	--	--	--	--
<b>Firm Transportation Keep-whole</b>					
Prices actively quoted	\$ (16)	\$ --	\$ --	\$ --	\$ (16)
Prices based on models and other valuation methods	--	(43)	(27)	(14)	(84)
<b>Total</b>					
Prices actively quoted	\$ (23)	\$ (1)	\$ --	\$ --	\$ (24)
Prices based on models and other valuation methods	--	(43)	(27)	(14)	(84)

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

### Capital Resources and Liquidity

#### Capital Expenditures\*

<i>millions</i>	Three Months Ended March 31	
	2002	2001
Development	\$ 308	\$ 353
Exploration	423	180
Acquisitions of producing properties	--	13
Gathering and other	1	25
Capitalized interest and exploration and development costs	81	87
<u>Total</u>	<u>\$ 813</u>	<u>\$ 658</u>

\* Excludes corporate acquisitions

During the first three months of 2002, Anadarko's capital spending (including capitalized interest and overhead) was \$813 million, an increase of 24% compared to the same period of 2001. This increase is primarily due to a \$243 million increase in exploration spending, partially offset by a \$45 million decrease in development spending. The shift in spending from development to exploration activities reflects the Company's decision to focus on increasing its inventory of drilling prospects by identifying new reserves through increased exploration, rather than growing production through development during the current down cycle for energy prices. The increase in exploration activity relates primarily to the higher level of activity in the Gulf of Mexico and Alaska.

**Debt** As of March 31, 2002, Anadarko's total debt was \$5.52 billion. This compares to total debt of \$5.05 billion at December 31, 2001. Due to activities in progress at the beginning of 2002 and the seasonal nature of drilling activity in Alaska and Canada, a disproportionate amount of the 2002 capital expenditure budget was spent in the first quarter of 2002 and, as a result, total debt increased \$0.47 billion.

In April 2002, Anadarko filed a shelf registration statement with the Securities and Exchange Commission that permits the issuance of up to \$1 billion in debt securities, preferred stock, preferred securities, depositary shares, common stock, warrants, purchase contracts and purchase units. Net proceeds, terms and pricing of the offerings of securities issued under the shelf registration statement will be determined at the time of the offerings.

In February 2002, the Company issued \$650 million principal amount of 5 3/8% Notes due 2007. In March 2002, the Company issued \$400 million principal amount of 6 1/8% Notes due 2012. The net proceeds from these issuances were used to reduce floating rate debt and to fund a portion of the Zero Yield Puttable Contingent Debt Securities (ZYP-CODES) put to the Company for repayment in March 2002.

In March 2001, Anadarko issued \$650 million of ZYP-CODES due 2021. Holders of the ZYP-CODES have the right to require Anadarko to purchase all or a portion of their ZYP-CODES in March 2002, 2004, 2006, 2011 or 2016, at \$1,000 per ZYP-CODES. In March 2002, ZYP-CODES in the amount of \$620 million were put to the Company for repayment and were paid in cash.

**Common Stock Purchase Program** In 2001, the Board of Directors authorized the Company to purchase up to \$1 billion in shares of Anadarko common stock. The share purchases may be made from time to time, depending on market conditions. Shares may be purchased either in the open market or through privately negotiated transactions. The repurchase program does not obligate Anadarko to acquire any specific number of shares and may be discontinued at any time.

To enhance the share repurchase program, Anadarko has sold put options to independent third parties. These put options entitle the holder to sell shares of Anadarko common stock to the Company on certain dates at specified prices. During 2001, Anadarko sold put options for the purchase of a total of 5 million shares of Anadarko common stock with a notional amount of \$240 million. Put options for 1 million shares were exercised and put options for 2 million shares expired unexercised in 2001. In January 2002, the Company entered into an additional put option for 1 million shares



## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

of Anadarko common stock with a notional amount of \$46 million and received a \$3 million premium. Put options for an additional 2 million shares expired unexercised in 2002. The remaining put option for 1 million shares will expire in July 2002, if not exercised. The put option permits a net-share settlement at the Company's option and does not result in a liability on the consolidated balance sheet as of March 31, 2002.

The following table summarizes purchases under the stock purchase program and the effect of the related put option premiums on the repurchase price.

<i>million, except per share amounts</i>	Annual 2001	First Quarter 2002	Total Program
Shares repurchased	2.2	1.0	3.2
Total paid for shares repurchased	\$ 116	\$ 50	\$ 166
Put premiums settled	(7)	(7)	(14)
Total repurchase price	\$ 109	\$ 43	\$ 152
Average repurchase price per share	\$ 49.41	\$ 43.04	\$ 47.42

### Obligations and Commitments

**Production Platform** In April 2002, the Company signed an agreement with El Paso Energy Partners (EPN) under which a floating production platform for its Marco Polo discovery in Green Canyon Block 608 of the Gulf of Mexico will be installed. EPN will construct the platform and processing facilities that upon completion, expected in 2004, will be operated by Anadarko. The agreement provides that Anadarko will dedicate its production from Green Canyon Block 608 and 11 other Green Canyon blocks to the processing facilities. The agreement will require a monthly demand charge of slightly over \$2 million for five years beginning at the time of project completion and a processing fee based upon production. Anadarko will be entitled to 25% of the net after tax cash proceeds from these facilities after payout, as defined, is attained. The agreement does not contain any purchase options, purchase obligations or value guarantees.

### Outlook on Liquidity

Anadarko's net cash from operating activities in the first quarter of 2002 was \$0.4 billion compared to \$1.1 billion in the first quarter of 2001. The decrease in cash flow is attributed primarily to a significant decrease in natural gas prices, as well as a decrease in crude oil, condensate and NGLs prices. The Company's original capital expenditure budget for 2002 was set at \$2.0 billion. The Company intends to adjust capital expenditures to reflect changes in its cash flow from operations. Cash flow from operations will vary depending upon, among other things, actual commodity prices received throughout the year.

Anadarko believes that operating cash flow and existing or available credit facilities will be adequate to meet its capital and operating requirements for 2002. However, due to activities in progress at the beginning of 2002 and the seasonal nature of drilling activity in Alaska and Canada, a disproportionate amount of the 2002 capital expenditure budget will be spent in the first and second quarters of the year. As a result, there will be an increase in debt in the first half of the year that the Company expects to reduce in the second half of 2002. Failure of prices to increase later in the year, as expected, could result in increased borrowing throughout the year. Reduced fourth quarter activity in 2002 relative to 2001 could lead to higher working capital requirements and also result in additional borrowing. The Company has a three-year stock buyback program to purchase up to \$1 billion in shares of Anadarko common stock. Anticipated stock repurchases for 2002 are not included in the announced capital expenditure budget and could require additional borrowing.

The Company's credit agreements allow for a maximum capitalization ratio of 60% debt, exclusive of the effect of any non-cash write-downs. As of March 31, 2002, Anadarko's capitalization ratio was 46% debt. While there is no specific restriction on paying dividends, under the maximum debt capitalization ratio retained earnings were not restricted as to the payment of dividends at March 31, 2002. The amount of future common stock dividends will depend on earnings, financial conditions, capital requirements and other factors, and will be determined by the Board of Directors on a quarterly basis.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

### Exploration and Development Activities

During the first quarter of 2002, Anadarko participated in a total of 356 wells, including 272 gas wells, 68 oil wells and 16 dry holes. This compares to a total of 243 wells, including 176 gas wells, 57 oil wells and 10 dry holes during the first quarter of 2001. Following are highlights of first quarter 2002 activity:

- In Algeria, production began from the fourth and final oil production train at the Hassi Berkine central processing facility (CPF). With the start-up of this train, which is capable of processing 75 MBbls/d of oil from five satellite fields in Block 404, gross oil production capacity through the CPF increased to 285 MBbls/d of oil.
- In North Louisiana, the Vernon field portion of the Bossier play has been expanded to become one of the Company's largest gas fields. Anadarko has increased gross production from 7 MMcf/d of gas when the field was acquired in December 1999 to approximately 78 MMcf/d of gas currently. New leasing and drilling has extended the field to the south and west. Five rigs are currently working in this area.
- In the Gulf of Mexico, Anadarko and El Paso Energy Partners signed an agreement under which a floating production platform for the Company's Marco Polo discovery at Green Canyon Block 608 will be installed. The facility design and construction has been contracted for, with installation planned for the third quarter of 2003 and start-up planned for the first quarter of 2004. At a water depth of 4,300 feet, Marco Polo will be the deepest tension-leg platform in the world. Six development wells are planned, with drilling scheduled to start in the second quarter of 2002.
- Also in the Gulf of Mexico, the "H" platform at the South Marsh Island 280-281 complex has been completed and production has reached 99 MMcf/d of gas and 1,000 barrels per day of oil from two discovery wells drilled in 2001. Anadarko has a 50% working interest in these wells. In the third quarter of 2002, the Company expects to install the "I" platform and bring on production from three other recent discoveries. All of these new wells are the result of a reappraisal and redevelopment program in this mature gas field.
- In Canada, the Company announced three significant natural gas discoveries. In northeast British Columbia, the Sahtaneh b-83 discovery well flowed at a rate of 10 MMcf/d of gas and the Adsett b-82-G, a Slave Point discovery, tested at 5 MMcf/d of gas before stimulation. In the Saddle Hills area of northern Alberta, the 15-28 discovery well was connected to the pipeline and is currently producing 9 MMcf/d of gas.
- Currently, there is political unrest in Venezuela, where the Company has a 45% participating interest in producing properties. Anadarko is presently unable to predict with certainty any effect the current situation may have on activity planned for 2002 and beyond. However, the situation has not had any material effect to date on the Company's operations.

### New Accounting Principles

*SFAS No. 143* SFAS No. 143, "Accounting of Asset Retirement Obligations," requires the fair value of a liability for an asset retirement obligation to be recorded in the period in which it is incurred and a corresponding increase in the carrying amount of the related long-lived asset and will be effective for the Company in January 2003. The Company is evaluating the impact of SFAS No. 143.

*SFAS No. 145* SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13 and Technical Corrections," was issued in April 2002. SFAS No. 145 provides guidance for income statement classification of gains and losses on extinguishment of debt and accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. SFAS No. 145 is effective for the Company in January 2003. The Company is evaluating the impact of SFAS No. 145.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

**Derivative Financial Instruments** Anadarko's derivative commodity instruments currently are comprised of futures, swaps and options contracts. The volume of derivative commodity instruments utilized by the Company to hedge its market price risk and in its energy trading operation can vary during the year within the boundaries of its established risk management policy guidelines.

Anadarko uses derivative financial instruments for various purposes and carefully monitors the credit worthiness of each counterparty. Derivative financial instruments utilized to manage or reduce commodity price risk related to the Company's equity production are accounted for under the provisions of Statement of Financial Accounting Standards No. 133 "Accounting for Derivative Instruments and for Hedging Activities." All derivatives are carried on the balance sheet at fair value. Realized gains/losses and option premiums are recognized in the statement of income when the underlying physical gas and oil production is sold. Accordingly, realized derivative gains/losses are generally offset by similar changes in the realized prices of the underlying physical gas and oil production. Realized derivative gains/losses are reflected in the average sales price of the physical gas and oil production.

Accounting for unrealized gains/losses is dependent on whether the derivative financial instruments have been designated and qualify as part of a hedging relationship. Derivative financial instruments may be designated as a hedge of exposure to changes in fair values, cash flows or foreign currencies, if certain conditions are met. Unrealized gains/losses on derivative financial instruments that do not meet the conditions to qualify for hedge accounting are recognized currently in earnings.

If the hedged exposure is to changes in fair value, the gains/losses on the derivative financial instrument, as well as the offsetting losses/gains on the hedged item, are recognized currently in earnings. Consequently, if gains/losses on the derivative financial instrument and the related hedge item do not completely offset, the difference (i.e., ineffective portion of the hedge) is recognized currently in earnings.

If the hedged exposure is a cash flow exposure, the effective portion of the gains/losses on the derivative financial instrument is reported as a component of accumulated other comprehensive income and reclassified into earnings in the same period or periods during which the hedged forecasted transaction affects earnings. The ineffective portion of the gains/losses from the derivative financial instrument, if any, as well as any amounts excluded from the assessment of the cash flow hedges' effectiveness are recognized currently in other (income) expense. Effective July 2001, the Company implemented Derivatives Implementation Group Issue G20, "Cash Flow Hedges: Assessing and Measuring the Effectiveness of a Purchased Option Used in a Cash Flow Hedge," which provides guidance for assessing the effectiveness on total changes in an option's cash flows rather than only on changes in the option's intrinsic value. Time value changes were previously being recognized in current earnings since the Company excluded time value changes from its assessment of hedge effectiveness.

If the hedged exposure is a foreign currency exposure, the accounting is similar to the accounting for fair value and cash flow hedges.

As of March 31, 2002, the Company had a net unrealized loss of \$26 million before taxes, or \$16 million after taxes, on derivative commodity instruments entered into to hedge equity production recorded in accumulated other comprehensive income. At December 31, 2001, the Company had a net unrealized gain of \$7 million before taxes (gains of \$9 million and losses of \$2 million), or \$4 million after taxes. Other income for the first quarter of 2002 and 2001, included \$11 million of net losses and \$9 million of net gains, respectively, related to derivative instruments designated as cash flow hedges. These gains/losses were primarily due to the change in the time value of the option contracts that was excluded from the assessment of hedge effectiveness, and the ineffective portion of the hedge. Based upon an analysis utilizing the actual derivative contractual volumes and assuming a 10% increase in commodity prices, the potential additional loss on these derivative commodity instruments would be approximately \$37 million.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)

As of March 31, 2002 and December 31, 2001, the Company had the following volumes under derivative contracts related to its oil and gas producing activities (non-trading activity). The difference between the fair values in the table and the unrealized gain (loss) recognized in accumulated other comprehensive income is due to premiums and ineffectiveness.

#### March 31, 2002

Production Period	Instrument Type**	Volumes (million MMBtu)	Average Price (\$ per MMBtu)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Natural Gas</b>				
2002	2-way collar*	1.7	3.00-5.00	\$ --
2002	3-way collar*	5.2	2.20-3.00-4.83	--
2002	Swaps*	30.6	3.09	(8)
2003	2-way collar*	2.3	3.00-5.00	--
2003	3-way collar*	6.8	2.20-3.00-4.83	(1)
2004	2-way collar*	2.3	3.00-5.00	--
2004	3-way collar*	6.9	2.20-3.00-4.83	(1)
2005	2-way collar*	2.3	3.00-5.00	--
2005	3-way collar*	6.8	2.20-3.00-4.83	(1)
2002	Calls sold	7.5	3.60	(2)
2002	Calls purchased	4.1	3.44	1
2003	Calls sold	7.4	3.15	(1)
2003	Calls purchased	10.2	3.31	1
2004	Calls sold	0.7	2.92	--
2004	Calls purchased	0.7	2.92	--
	Total			\$ (12)

Production Period	Instrument Type**	Volumes (MMBbls)	Average Price (\$ per barrel)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Crude Oil</b>				
2002	Swaps*	4.3	24.58	\$ (4)
2002	2-way collar*	1.1	22.30-23.32	(3)
2002	3-way collar*	5.1	17.96-22.05-28.11	(5)
2003	Swaps*	0.8	23.80	--
2003	2-way collar*	0.4	22.30-23.32	(1)
2003	3-way collar*	3.7	17.00-21.00-26.33	(3)
	Total			\$ (16)

### Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)

December 31, 2001

Production Period	Instrument Type**	Volumes (million MMBtu)	Average Price (\$ per MMBtu)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Natural Gas</b>				
2002	2-way collar*	2.3	3.00-5.00	\$ 1
2002	3-way collar*	6.8	2.20-3.00-4.83	2
2003	2-way collar*	2.3	3.00-5.00	1
2003	3-way collar*	6.8	2.20-3.00-4.83	1
2004	2-way collar*	2.3	3.00-5.00	1
2004	3-way collar*	6.9	2.20-3.00-4.83	1
2005	2-way collar*	2.3	3.00-5.00	1
2005	3-way collar*	6.8	2.20-3.00-4.83	1
2002	Calls sold	10.1	3.66	2
2002	Calls purchased	4.9	3.50	--
2003	Calls sold	7.4	3.18	(2)
2003	Calls purchased	10.2	4.12	2
2004	Calls sold	0.7	2.95	--
2004	Calls purchased	0.7	2.95	--
	Total			\$ 11
Production Period	Instrument Type**	Volumes (MMBbls)	Average Price (\$ per barrel)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Crude Oil</b>				
2002	Swaps*	0.4	25.56	\$ 2
2002	3-way collar*	3.3	19.11-23.33-30.51	6
	Total			\$ 8

MMBtu - million British thermal units

MMBbls - million barrels

\* Qualifies for hedge accounting.

\*\* A "2-way collar" is a combination of options, a sold call and purchased put. The purchased put establishes a minimum price (the "floor") and the sold call establishes a maximum price (the "ceiling") the Company will receive for the volumes under contract. A "3-way collar" is a combination of options, a sold call, a purchased put and a sold put. The purchased put establishes a minimum price unless the market price falls below the sold put, at which point the minimum price would be New York Mercantile Exchange plus the difference between the purchased put and the sold put strike price. The sold call establishes a maximum price (the "ceiling") the Company will receive for the volumes under contract.

Derivative financial instruments utilized in the Company's energy trading activities and in the management of price risk associated with the Company's firm transportation keep-whole commitment are accounted for under the mark-to-market accounting method pursuant to Emerging Issues Task Force Issue 98-10, "Accounting for Contracts Involved in Energy Trading and Risk Management Activities." Under this method, the derivatives and physical delivery purchase and sale contracts are revalued in each accounting period and premiums and unrealized gains/losses are immediately recorded in the statement of income and carried as assets or liabilities on the balance sheet. Anadarko's energy marketing and trading business is backed by the Company's substantial oil and gas production and reserves. In the United States and Canada, the Company purchases natural gas produced by other companies in those areas where the Company has substantial production volumes. Third-party purchases allow the Company to aggregate larger volumes of gas and attract larger, more creditworthy customers, which in turn spreads the Company's relatively fixed overhead costs over more gas and can help reduce transportation costs. The Company does not engage in market making practices nor does it trade in any non-energy-related commodities. The marketing and trading business's risk position, most of the time, is a net short position. Excluding the firm transportation keep-whole agreement, essentially all of the Company's trading transactions have a term of less than one year and most are less than three months. The keep-whole

### Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)

agreement will be in effect until the earlier of each contract's expiration date or February 2009. As of March 31, 2002, the Company had a net unrealized loss of \$3 million (gains of \$34 million and losses of \$37 million) on derivative commodity instruments entered into for trading purposes and a net unrealized loss of \$5 million (gains of \$16 million and losses of \$21 million) on physical contracts entered into for trading purposes. As of December 31, 2001, the Company had a net unrealized loss of \$49 million (gains of \$42 million and losses of \$91 million) on derivative commodity instruments entered into for trading purposes. Losses on derivative commodity instruments were offset by a net unrealized gain of \$66 million (gains of \$82 million and losses of \$16 million) on physical contracts entered into for trading purposes. Based upon an analysis utilizing the actual derivative contractual volumes and assuming a 10% increase in underlying commodity prices, the potential loss on the derivative instruments would be decreased by approximately \$10 million.

The energy trading derivative contracts are primarily used to neutralize fixed price exposure in physical delivery agreements and to generate profit on or from exposure to changes in the market price of crude oil and natural gas. As of March 31, 2002 and December 31, 2001, the Company had the following volumes under derivative contracts related to its trading activity:

#### March 31, 2002

Production Period	Instrument Type	Volumes (million MMBtu)	Average Price (\$ per MMBtu)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Natural Gas</b>				
2002	Futures sold	15.4	2.88	\$ (9)
2002	Futures purchased	16.8	3.18	5
2002	Swaps	45.6	3.31	1
2002	Calls sold	3.1	2.75	--
2002	Calls purchased	5.3	3.59	--
2002	Puts sold	6.6	3.05	(2)
2002	Puts purchased	3.5	2.54	--
2003	Futures sold	4.7	3.47	(2)
2003	Futures purchased	6.2	3.52	2
2003	Swaps	20.2	3.45	5
2004	Futures sold	0.5	3.84	--
2004	Swaps	0.2	3.89	--
2005	Swaps	1.0	3.78	--
2006	Swaps	0.6	3.69	--
	Total			\$ --

Production Period	Instrument Type	Volumes (MMBbls)	Average Price (\$ per barrel)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Crude Oil</b>				
2002	Futures sold	2.1	22.44	\$ (7)
2002	Futures purchased	2.1	21.44	5
2002	Swaps	0.1	19.76	(1)
2002	Calls sold	0.3	23.50	--
2002	Calls purchased	0.2	24.00	--
2002	Puts sold	0.2	20.50	--
2002	Puts purchased	0.2	20.50	--
	Total			\$ (3)

### Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)

**December 31, 2001**

Production Period	Instrument Type	Volumes (million MMBtu)	Average Price (\$ per MMBtu)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Natural Gas</b>				
2002	Futures sold	23.8	3.34	\$ 18
2002	Futures purchased	22.3	3.50	(21)
2002	Swaps	72.3	3.20	(42)
2002	Calls sold	8.5	3.07	1
2002	Calls purchased	12.8	4.09	1
2002	Puts sold	8.3	3.25	(7)
2002	Puts purchased	0.8	2.58	--
2003	Futures sold	1.2	3.51	--
2003	Futures purchased	0.3	3.36	--
2003	Swaps	12.2	3.12	--
	Total			<u>\$ (50)</u>

Production Period	Instrument Type	Volumes (MMBbls)	Average Price (\$ per barrel)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Crude Oil</b>				
2002	Futures sold	2.8	19.80	\$ (1)
2002	Futures purchased	1.5	20.05	2
2002	Swaps	0.5	21.77	--
2002	Calls sold	0.4	29.50	--
	Total			<u>\$ 1</u>

RME Holding Company (RME) was a party to several long-term firm gas transportation agreements that supported their gas marketing program within the gathering, processing and marketing (GPM) business segment, which was sold in 1999 to Duke Energy Field Services, Inc. (Duke). Most of the GPM's firm long-term transportation contracts were transferred to Duke in the GPM disposition. One contract was retained, but is managed and operated by Duke. Anadarko is not responsible for the operations of the contracts and does not utilize the associated transportation assets to transport the Company's natural gas. As part of the GPM disposition, RME agreed to pay Duke if transportation market values fall below the fixed contract transportation rates, while Duke will pay RME if the transportation market values exceed the contract transportation rates (keep-whole agreement). Net (payments) to or receipts from Duke for the three months ended March 31, 2002 and 2001 were \$(10) million and \$76 million, respectively. Transportation contracts transferred to Duke in the GPM disposition and the contract not transferred, all of which are included in the keep-whole agreement with Duke, relate to various pipelines. This keep-whole agreement is accounted for on a mark-to-market basis. This keep-whole agreement will be in effect until the earlier of each contract's expiration date or February 2009. During the first quarter of 2002, the Company recognized other expense of \$6 million (\$3 million from the agreement and \$3 million from derivative financial instruments). During the first quarter of 2001, the Company recognized other income of \$140 million (\$183 million from the agreement and \$(43) million from derivative financial instruments). As of March 31, 2002, other current liabilities included \$23 million and other long-term liabilities included \$77 million related to this agreement. As of December 31, 2001, other current liabilities included \$27 million and other long-term liabilities included \$80 million related to this agreement. The future gain or loss from this agreement cannot be accurately predicted.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)

Anticipated discounted and undiscounted liabilities for the firm transportation keep-whole commitment at March 31, 2002 are as follows:

<i>millions</i>	March 31, 2002	
	Undiscounted	Discounted
2002	\$ 16	\$ 16
2003	23	21
2004	27	22
2005	20	15
2006	19	12
Later years	23	14
Total	<u>\$ 128</u>	<u>\$ 100</u>

The Company may periodically use derivative financial instruments to reduce its exposure under the keep-whole agreement to potential decreases in future transportation market values. While the derivatives are intended to reduce the Company's exposure to declines in transportation market rates, they also limit the potential to benefit from market price increases. For the three months ended March 31, 2002 and 2001, the Company recognized other expense of \$3 million and \$43 million, respectively, on derivative financial instruments related to transportation rates. At March 31, 2002 and December 31, 2001 other current assets included zero and \$25 million, respectively, of unrealized gains related to this agreement. Due to decreased liquidity, the use of derivative financial instruments to manage this risk is generally limited to the forward twelve months only.

As of March 31, 2002, the Company had no volumes under derivative contracts related to the firm transportation keep-whole agreement. As of December 31, 2001, the Company had the following volumes under derivative contracts related to the firm transportation keep-whole agreement:

#### December 31, 2001

Production Period	Instrument Type	Volumes (million MMBtu)*	Average Price (\$ per MMBtu)	Net Fair Value Asset (Liability) <i>millions</i>
<b>Natural Gas</b>				
2002	Swaps	4.2	8.42	\$ 25

\* Represents 2% of the Company's total volumetric exposure under the keep-whole agreement for 2002.

For additional information regarding the Company's marketing and trading portfolio and the firm transportation keep-whole agreement see [Marketing Strategies](#) under Item 2 of this Form 10-Q.



### Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)

**Common Stock Purchase Program** In 2001, the Board of Directors authorized the Company to purchase up to \$1 billion in shares of Anadarko common stock. The share purchases may be made from time to time, depending on market conditions. Shares may be purchased either in the open market or through privately negotiated transactions. The repurchase program does not obligate Anadarko to acquire any specific number of shares and may be discontinued at any time. During 2001, the Company purchased 2.2 million shares of common stock for \$116 million. In January 2002, the Company purchased an additional 1 million shares of common stock for \$50 million.

To enhance the share repurchase program, Anadarko has sold put options to independent third parties. These put options entitle the holder to sell shares of Anadarko common stock to the Company on certain dates at specified prices. During 2001, Anadarko sold put options for the purchase of a total of 5 million shares of Anadarko common stock with a notional amount of \$240 million. Put options for 1 million shares were exercised and put options for 2 million shares expired unexercised in 2001. In January 2002, the Company entered into an additional put option for 1 million shares of Anadarko common stock with a notional amount of \$46 million and received a \$3 million premium. Put options for an additional 2 million shares expired unexercised in 2002. The remaining put option for 1 million shares will expire in July 2002, if not exercised. The put option permits a net-share settlement at the Company's option and does not result in a liability on the consolidated balance sheet as of March 31, 2002.

**Foreign Currency Risk** The Company's Canadian subsidiaries use the Canadian dollar as their functional currency. The Company's other international subsidiaries use the U.S. dollar as their functional currency. To the extent that business transactions in these countries are not denominated in the respective country's functional currency, the Company is exposed to foreign currency exchange rate risk. In addition, in these subsidiaries, certain asset and liability balances are denominated in currencies other than the subsidiary's functional currency. These asset and liability balances are remeasured in the preparation of the subsidiary's financial statements using a combination of current and historical exchange rates, with any resulting remeasurement adjustments included in net income during the period.

At March 31, 2002 and December 31, 2001, a Canadian subsidiary had \$187 million outstanding of fixed-rate notes and debentures denominated in U.S. dollars. During the first quarter of 2002 and 2001, the Company recognized zero and \$33 million, respectively, of non-cash losses before taxes associated with the remeasurement of this debt. The potential foreign currency remeasurement impact on earnings from a 10% change in the March 31, 2002 Canadian exchange rate would be about \$19 million based on the outstanding debt at March 31, 2002.

The Company periodically enters into foreign currency contracts to hedge specific currency exposures from commercial transactions. The Company has acquired foreign currency forward exchange contracts with maturities through October 2004 and recorded a \$4 million deferred liability representing the fair value of these contracts. These contracts were determined to be cash flow hedges of Anadarko Canada's future U.S. dollar denominated hydrocarbon sales. This deferred liability will be recognized in earnings when the contracts are settled. The unrealized loss on foreign currency contracts excluding the \$4 million unamortized deferred liability as of March 31, 2002 and December 31, 2001 was \$6 million. Approximately \$3 million of the after tax unrealized loss was included in accumulated other comprehensive income as of March 31, 2002 and December 31, 2001. No portion of the balance is expected to be reclassified into earnings during 2002.

The following table summarizes the Company's open foreign currency positions at March 31, 2002 and December 31, 2001:

<i>\$ in millions, except foreign currency rates</i>	March 31, 2002	December 31, 2001
Notional amount - US\$	\$ 70	\$ 70
Forward rate	1.36	1.36
Market rate	1.58	1.58
Decrease in rate	(0.22)	(0.22)
Fair value - loss - C\$	\$ 15	\$ 15
Fair value - loss - US\$	\$ 10	\$ 10

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk (continued)**

At March 31, 2002 and December 31, 2001, the Company's Latin American subsidiaries had foreign deferred tax liabilities denominated in the local currency equivalent totaling \$66 million and \$78 million, respectively. During the first quarter of 2002 and 2001, the Company recognized tax benefits associated with remeasurement of these deferred tax liabilities of \$13 million and zero, respectively. In conjunction with the sale of Latin American properties in 2001, the Company indemnified a purchaser for the use of local tax losses denominated in the local currency equivalent totaling \$22 million. The potential foreign currency remeasurement impact on net earnings from a 10% change in the March 31, 2002 Latin American exchange rates would be approximately \$8 million.

**Interest Rate Risk** Anadarko is also exposed to risk resulting from changes in interest rates as a result of the Company's variable and fixed interest rate debt. The Company believes the potential effect that reasonably possible near term changes in interest rates may have on the fair value of the Company's various debt instruments is not material.

## Part II. OTHER INFORMATION

### Item 1. Legal Proceedings

See [Note 13](#) of the Notes to Consolidated Financial Statements under Part I - Item 1 of this Form 10-Q.

### Item 6. Exhibits and Reports on Form 8-K

#### (a) Exhibits

Exhibits not incorporated by reference to a prior filing are designated by an (\*) and are filed herewith; all exhibits not so designated are incorporated herein by reference to a prior filing as indicated.

<u>Exhibit Number</u>	<u>Description</u>	<u>Original Filed Exhibit</u>	<u>File Number</u>
3(a)	Restated Certificate of Incorporation of Anadarko Petroleum Corporation, dated August 28, 1986	4(a) to Form S-3 dated May 9, 2001	333-60496
(b)	By-laws of Anadarko Petroleum Corporation, as amended	3(e) to Form 10-Q for the quarter ended September 30, 2000	1-8968
(c)	Certificate of Amendment of Anadarko's Restated Certificate of Incorporation	4.1 to Form 8-K dated July 28, 2000	1-8968
4(a)	Certificate of Designation of 5.46% Cumulative Preferred Stock, Series B	4(a) to Form 8-K dated May 6, 1998	1-8968
(b)	Rights Agreement, dated as of October 29, 1998, between Anadarko and The Chase Manhattan Bank	4.1 to Form 8-A dated October 30, 1998	1-8968
*12	Computation of Ratios of Earnings to Fixed Charges and Earnings to Combined Fixed Charges and Preferred Stock Dividends		

#### (b) Reports on Form 8-K

A report on Form 8-K dated January 30, 2002 was filed in which the earliest event reported was January 29, 2002. This event was reported under Item 5 "Other Events" and Item 7(c), "Exhibits."

A report on Form 8-K dated February 22, 2002 was filed in which the earliest event reported was February 22, 2002. This event was reported under Item 5 "Other Events" and Item 7(c), "Exhibits."

A report on Form 8-K dated March 8, 2002 was filed in which the earliest event reported was March 8, 2002. This event was reported under Item 5 "Other Events" and Item 7(c), "Exhibits."

## **SIGNATURES**

**Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned duly authorized officer and principal financial officer.**

**ANADARKO PETROLEUM CORPORATION**

(Registrant)

May 10, 2002

By: MICHAEL E. ROSE  
Michael E. Rose - Executive Vice President,  
Finance and Chief Financial Officer